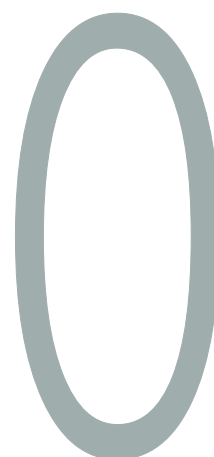


ANNUAL REPORT

OF THE BANK OF ALBANIA



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Governor of the Bank of Albania, Mr. Ardian Fullani.



Bank of Albania Supervisory Council

From left to the right in front:

KSENOFON KRISAFI
ARDIAN FULLANI
TEFTA ÇUÇI
FATOS İBRAHIMI

Member
Chairman (Governor of the Bank of Albania)
Member
Vice Chairman (First Deputy Governor)

From left to the right in the back:

LIMOS MALAJ
ARJAN KADAREJA
ADRIAN CIVICI
HALIT XHAFA
BENET BECI

Member
Member
Member
Member
Member

FOREWORD BY THE GOVERNOR

Dear reader,

It is a special pleasure to meet with you again, in this annual presentation of the performance of Albania's economy and Bank of Albania's work, not only for the fulfilment of its legal mandate, but also for the development of its institutional commitments.

Bank of Albania's Annual Report is a true statement of the opinion of the institution I govern, about the economic developments during the year, the problems, challenges and measures taken for maintaining the macroeconomic and financial balances, improving the economic development infrastructure, developing the money market and encouraging the financial intermediation as well as for a broader and transparent communication with the public.

The Albanian economy was generally characterised by positive developments throughout 2008. The economic growth was in line with projections and the macroeconomic balances remained robust. In particular, the Bank of Albania has achieved its primary target for maintaining price stability, contributing to an average inflation rate of 3.4 percent along 2008.

However, in the chronological aspect, the country's economy development has gone through two distinct phases during the year. The first nine-month period of the year performed in the context of a fairly positive global climate, particularly in our partner countries. Responding to high lending rates, this period was associated not only with a high domestic demand and strong economic growth, but also with boosted inflationary pressures and growth of both, trade deficit and current account balance. Consumption and investment were high during this period. In the meantime, the last quarter of the year was characterised by an increasing impact of the economic and financial global crisis on the country's economy. The global crisis was reflected in shaking the economic agents' confidence in the banking system and emerging liquidity problems in it. They were also associated with a deceleration of the growth of the economic activity and financial intermediation at home. These developments highlighted the importance of preserving financial system's stability and macroeconomic balances, in view of establishing the grounds for a long-term and a sustainable economic growth. These problems will constitute the subject of economic policies throughout 2009 and onward.

From the institutional viewpoint, year 2008 was characterised by intensification of our endeavours to create the infrastructure and the regulatory base needed for the development of the country's economy. Significant achievements were highlighted in terms of strengthening the analytical and decision-making capacities of the Bank of Albania, reviewing and strengthening the prudential

regulations, completing the legal and regulatory framework of the development of the banking system, developing the interbank market and enhancing our intervention instruments, upgrading the payment system, enhancing Bank of Albania's communication with the public, etc. All these developments have been transparently reflected in the pages of this Annual Report.

Being grateful to the devoted Bank of Albania staff for its accomplishments and confident that year 2009 will record further steps in institutional strengthening and enhancement of Bank of Albania's capacities, I thank you for your attention and interest in the activity of this institution. In the following, I invite you to get acquainted with core economic and institutional development analyses for 2008.

ARDIAN FULLANI



Governor

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CHAPTER I DEVELOPMENTS IN FOREIGN MARKETS AND ECONOMIES

1.1 WORLD ECONOMY

World growth decelerated in 2008, recording 3.4 percent, well below the 5 percent average growth registered in four previous years. This downturn was affected by the aftermath of the financial crisis that originated in the USA in 2007 and escalated sharply in mid 2008, spreading to developed European economies and later on to the Central and Eastern European countries.

Mortgage market collapse led to ongoing decline of financial stock prices, making crisis spread to other segments of the economy. These conditions made the decision-making institutions apply easing monetary policies to give some more space to the market, and launch fiscal stimulus packages to boost public confidence in the financial system, thus helping banks and other large industries escape from breakdown difficulties, in some cases even nationalizing some of them.

Inflationary pressures were high during the first half of the year, easing during the rest of it. Average inflation at global level picked up to 3.5 percent in 2008, from 2.1 percent in 2007, consequent to rapid food and energy price rise, fuelled by a decreased supply and a relatively high demand in the first half of the year. Influenced by the evolving financial crisis over the second half of 2008, prices followed a downward trend, envisaged to continue even during 2009.

Countries	GDP growth		Annual unemployment rate		Annual inflation rate	
	2007	2008	2007	2008	2007	2008
USA	2.0	1.1	4.6	5.8	2.9	3.8
Euro-zone	2.7	0.9	7.5	7.5	2.1	3.3
Germany	2.5	1.3	8.4	7.3	2.3	2.8
Greece	4.0	2.9	8.3	8.3 ¹	3.0	4.2
Italy	2.9	-0.6 ¹	6.1	6.7 ¹	2.0	3.5
Japan	1.9	-0.6	3.9	4.0	0.0	1.4

Source: European Commission, Eurostat, Respective statistical Institutes

Table 1 Key macroeconomic indicators

1.1.1. THE EURO-ZONE ECONOMY

The Euro-zone growth decelerated in 2008, recording about 0.9 percent, relative to 2.7 percent in 2007. Year 2008 was featured by slowed domestic demand and private investments, tighter credit conditions, increased unemployment rate and decreased consumer and business confidence indicators.

The highest growth rate of the Euro-zone was noted over the first quarter, when the financial crisis was not intensified yet. Increased consumption spending and positive developments in construction contributed to this growth. During the three following quarters, the Euro-zone recorded contraction, thus entering into technical recession. This economic slowdown was consequent to the financial crisis and its spillovers to the economy, turning the housing market down and leading some large financial institutions to bankruptcy. Notwithstanding the support measures taken by the ECB, the growth in domestic demand and in private investments significantly decelerated.

Annual inflation of the Euro-zone averaged 3.3 percent in 2008, which is significantly above the 2 percent upper limit of the ECB. The driving force behind higher inflation was higher energy and processed food prices¹. Inflation rate underwent an upward trend, peaking at 3.8 percent in August and declining steadily in the second half of the year.

1.1.2. U.S. ECONOMY

Following some years of moderate GDP growth, in 2008 the economic activity of the United States of America was characterised by a downswing. Declining stock market prices, deteriorating balance sheets of several large financial firms and tumbling home prices affected the real economy performance. Tight conditions for extending new credit and the effect of household and corporate nominal assets depreciation dropped the consumer and business confidence indicators and aggregate investments.

In the first half of the year, the Federal Government took some fiscal stimulus measures, aiming at maintaining an increase in consumer spending. Coupled with improved external demand because of US dollar's depreciation against some main international currencies, those administrative measures helped GDP grow at relatively high rates². Accelerated lost loans rise over the second half of the year negatively impacted on the balance sheets of several financial institutions, peaking with the bankruptcy of some of them. In consequence, the interbank market was faced with liquidity constraints and banks were obliged to further tighten their lending terms. Aggregate investments and consumer spending, i.e., two main components in estimating GDP, dropped rapidly in annual terms. Both above indicators, coupled with aggregate export plunge due to the US dollar's appreciation and decreased global demand, caused contraction of the American economy in last two quarters of the year.

Unfavourable data on manufacturing industry impacted on the worsening of employment figures in the economy. The average number of unemployed americans soared to about 25 percent in 2008 relative to 2007, mainly due to increased unemployment in manufacturing, construction and financial sectors.

Ongoing oil, energy and raw materials price rise in the first half of the year drove up the accelerating inflation rate during January to August. In

the meantime, the reverse price performance of these products led to falling consumer price index over the last months of the year.³

1.1.3. BRIC ECONOMIES⁴

BRIC countries were also affected by the economic slowdown of advanced countries, mainly in the second half of the year. Their ever-larger economic and financial integration across various regions of the world made possible that the financial turmoil, the rise and then the fall of oil and raw materials prices, as well as investors' and businesses' lack of confidence, conditioned the economic performance of the BRIC countries.

Countries	2007	2008	2007	2008
	INFLATION		REAL ECONOMIC GROWTH	
Brazil	6.4	5.7	5.4	6.3 ²
China	2.4	6.5 ¹	11.9	9.0
India	10.5	8.2	9.3	8.1 ²
Russia	13.8	14.1	8.1	7.7 ²

Source: IMF, OECD, Respective statistical institutes

¹Average rate for 11 first months of 2008

²Average rate for first three quarters of 2008

Table 2 Some macroeconomic indicators of BRIC countries

Nevertheless, the decreased raw materials prices weakened some of industrial output indicators and slowed down the export growth in the second half of the year. In Brazil, the economy grew at comparably high rates over 2008. Aggregate investments and consumer spending continued to grow at accelerated rates, but also generated ongoing and prolonged inflationary pressures.

Russia was faced with accelerated depreciation of stock-exchange and national currency vis-à-vis the main international currencies. After a period when the economy benefited from high oil and energy prices, given Russia's position as an exporting country of such resources, the accelerated price cut in the second half of the year led to decreased domestic demand and deteriorated current account. Inflation rate reflected a downward trend during the last months of the year, but, however, it stood at high rates.

In India, the deceleration in the domestic demand growth under the conditions of inflation rate upswing and reduced production capacities of domestic companies affected the slowdown of GDP growth.

During 2008 the China's economy was faced with a weakened growth rate of external demand, though it recorded a two-digit growth rate of 17.2 percent⁵. This was due to dampened domestic demand in advanced economies, thus rendering a substantial contribution to moderating the economic growth rates for 2008. In order to preserve the positive performance of consumer spending, the Chinese Government undertook several fiscal policies in the form of public investments and individual tax cut.

1.1.4. THE ECONOMY OF REGIONAL COUNTRIES

• ITALY

During 2008 the Italian economy performance was conditioned by the global financial turmoil. GDP contracted by 0.6 percent in annual terms, compared to 2007, due to decreased domestic demand and investments. Fast depreciation of financial assets, decreased real disposal income of individuals and households and the fear for deterioration of employment indicators led to a sluggish consumer spending⁶. The Euro's depreciation was not sufficient to buffer out the reduced demand for Italian exports in the markets inside and outside the European Union. However, the reduction of aggregate imports at more accelerated paces helped rendering a positive contribution of net exports to GDP estimate.

High raw materials prices and weak demand for Italian goods and services conditioned the economic activity in the manufacturing industry. During 2008, the industrial production dropped on average 4 percent, compared to the previous estimate. Data on construction industry show reduced total production capacity, while the average buildings price has not followed the downturn that characterised the Euro-zone States over this year. The average inflation rate for 2008 was 3.5 percent, with its highest rates over the first half of the year.

• GREECE

The Greek economy was resilient to the economic turmoil that has affected the industrialised countries. In 2008 the GDP growth rate was higher than that of the Euro-zone, recording 2.9 percent. This is attributed to constant increase in consumer spending and moderate export growth in goods and services, regardless of decreased aggregate investments⁷.

Consumer credit, extended mainly for new house purchases or for business, dropped during 2008, a fact confirmed also by the decline in business and consumer confidence indexes over this year. Hence, the industrial production fell by 3.7 percent in annual terms, consequent to weakened activity in processing industry and energy. In contrast, construction continued to grow on annual basis, though at more moderate paces than the previous year. Inflation rate was rising until September, when pressures on this indicator started to dampen⁸.

Table 3 Regional economic indicators during 2008

Countries	GDP growth	Annual inflation	Unemployment rate	Current account ³	Budget deficit ³
Italy	-0.6 ¹	3.5	6.7 ¹	-2.2	-2.8
Greece	2.9	4.2	8.3 ¹	-13.4	-3.4
Macedonia	5.8 ²	8.3	33.9 ²	-12.9 ⁴	3.0 ⁴
Serbia	6.1	13.6	14.2 ²	-20.7 ⁵	-0.3 ⁴
Croatia	3.1 ²	6.1	13.3	-10.9 ⁴	-2.1 ¹
Turkey	3.2 ²	10.4	15.2 ²	-6.0 ⁴	-1.4 ¹

Source: Respective statistical institutes, Eurostat, European Commission.

¹ 2008 estimates

² Average rate for the first three quarters of 2008

³ As a share of GDP

⁴ The figure for the third quarter of 2008

⁵ The figure for the second quarter of 2008

- *FYROM ECONOMY*

The FYROM economic growth rate for the first nine-month period of 2008 posted on average 5.7 percent, slightly higher than the 5.5 percent rate recorded in the first nine-month period of 2007. Production and construction sectors were the main contributors to the formation of this indicator, while agricultural production growth was lower than the economic growth rate.

Inflationary pressures were high during 2008. Inflation rate was 8.3 percent, compared to 2.3 percent in 2007. This rise was driven by fast rise of food and energy prices, consequent to unfavourable weather conditions.

- *TURKEY*

Turkish economy growth decelerated during the first nine-month period of 2008, averaging to 3.2 percent, compared to about 5 percent during the same period of 2007. This deceleration was due to reduced growth rates in private investments and in consumer spending. Projections speak for lower growth rates over the fourth quarter of the year, which is expected to continue in the course of 2009.

Annual inflation in Turkey recorded 10.4 percent during 2008, from 8.3 percent in the previous year. Energy and processed food prices rose significantly. Inflationary pressures were dampened during the last months, when December recorded negative annual rates, due to price cut of clothes and house rents.

1.2 MONETARY POLICY OF MAIN CENTRAL BANKS AND FINANCIAL MARKET DEVELOPMENTS

During 2008 the financial markets were unusually, largely and dramatically volatile, due to restructuring of financial institutions' balance sheets and agents' reaction, following the uncertainty brought about by the financial turbulence ignited in 2007. This sensation affected almost all financial market segments. The largest shock occurred in the third quarter, when the Lehman Brothers collapse was posted in September 2008, which made stock exchanges crash and volatility go through historical highs.

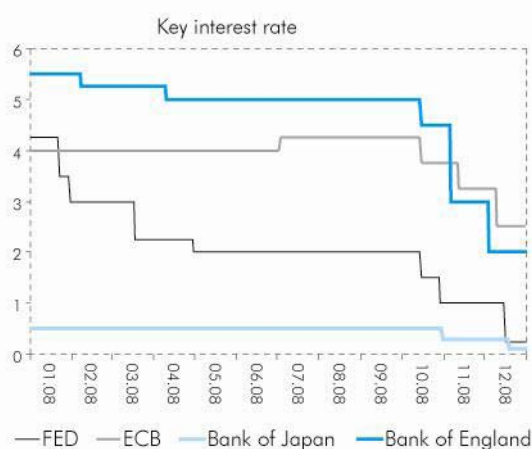
Aiming at relaxation and normalization of these pressures in the global financial markets, the monetary authorities took coordinated and immediate measures⁹. Some of them cut interest rates to the lowest historical rates. Positive raw materials price performance changed the focus of these authorities from anti-inflationary policies into easing ones, aiming at mitigating the cost of money for financial institutions.

The Central European Bank changed the key interest rate four times during 2008. On July 2008 the interest rate was raised by 0.25 percentage points, in an effort to monitor the inflationary pressures signalled by the developments over the first half of the year. During the last quarter, monetary policy stance

changed on the easing side and the key interest rate was cut twice by 0.50 percentage point and once by 0.75 percentage point. In January 2008, the key interest rate was 4.0 percent, whereas in December it recorded 2.5 percent.

The Federal Reserve cut the interest rate seven times during 2008, to 0-0.25 percent, from 4.25 percent at the year-start. Interest rate dropping to minimum historical rates took place in an effort to promote the lending activity, which was downward in the wane of the US financial problems.

Chart 1 Key interest rate performance in large economies

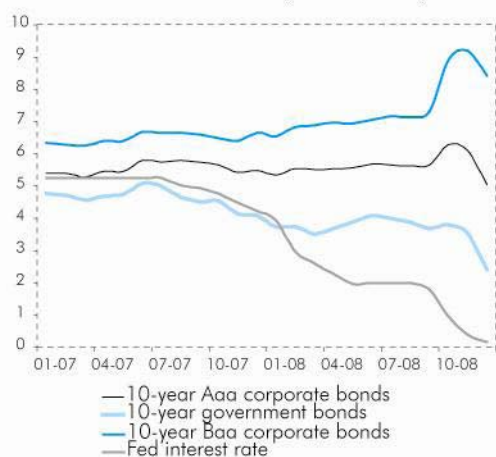


The Bank of England also undertook an easing monetary policy, lowering the interest rate for the fifth time, to 3.0 percent from 5.5 percent it was at the year-start. These decisions were made in an effort to buffer out the spillovers stemming from the financial market developments and to restrain the economic slowdown.

Notwithstanding the limited space, the Bank of Japan lowered the interest rate with two consecutive moves, by 0.2 percentage point, to 0.1 percent in December. This move occurred after the forecasting of further economic slowdown in Japan for 2009.

With both the monetary and fiscal stimulus, the interest rates in international financial markets dropped over the year-end 2008. Thus, during the last months of the year, the interbank market interest rates dropped significantly, reflecting the key interest rate cuts of respective central banks. Notwithstanding the interest rate reduction in those markets, the tension and risk perception by participants remain at high levels. This is reflected in high volumes of liquidity not used in the form of overnight deposits, and in high interest rate dynamics applied in those markets for exchanging unsecured funds. Hence, the spread between the US government treasury bill rate and the LIBOR rate in good economic times is estimated to range between 25-50 basis points. After the first signs of the financial crisis were evidenced in summer 2007, this spread increased by around 100 basis points, reaching record levels in late September by 487 basis points.

Chart 2 Yield performance of several securities in the US market (2007-2008)



In line with interest rate cut by the Fed to 0.00 - 0.25 percent, the US government treasury bills interest rates dropped further. During last months of the year, a negative interest rate was recorded in some cases. Corporate bonds market testified a correction of investors' preferences, leading to credit risk rating review. Increased demand for

bonds regarded by the lending agencies as safer, was reflected in a higher *yield* on average for 2008. This fact testifies lack of investors' confidence in the wane of worsening financial statements of larger US financial companies and ongoing loss of their assets value.

Another development worthy of note is the impact of weakening real economies of some advanced Eastern European countries on the financial markets. Countries such as Hungary, Czech Republic, Poland or Rumania experienced an ongoing increase of the budget deficit, depreciation of their national currencies and reduction of foreign direct investments in 2008. Furthermore, their financial problems, coupled with application for debt approval by several main international financial institutions, influenced the reviewing of their government treasury bills rating. Hence, the ratings agency lowered Hungary's treasury bill rating level in November 2008, whereas the Czech Republic and Poland government bonds were somewhat more stable.

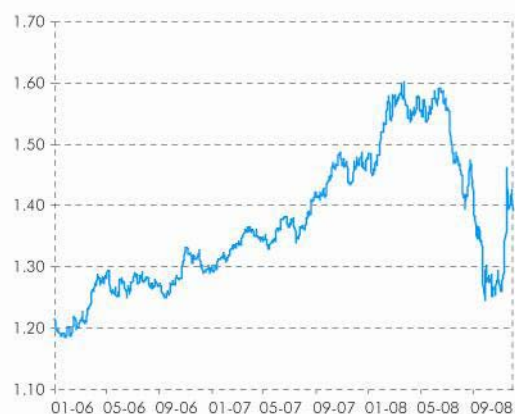
In international forex markets, in the course of 2007 and early 2008 the short (selling) position of the US dollar seemed as the most appropriate solution, since it was depreciated throughout this period by 13 percent vis-à-vis the Euro and by 10 percent and 8.5 percent vis-à-vis the Japanese Yen and the British pound respectively. The positive performance of the euro/USD ratio during the first half of the year is attributed to the positive performance of macroeconomic indicators in the Euro-zone and the tightening policies (base rate rise) of the European monetary authority, in contrast to the American one (base rate cut), making this ratio be traded at 1.579 maximum value.

The US dollar was boosted from August until the end of 2008, being appreciated by 2.9 percent against other major currencies and by 4.2 percent against the euro. The high demand for the American dollar by many financial institutions, non-positive performance of the Euro-zone's economy and the latest data of some macroeconomic indicators beyond market agents' expectations, led to such developments.

1.3 RAW MATERIALS PRICES IN INTERNATIONAL MARKETS

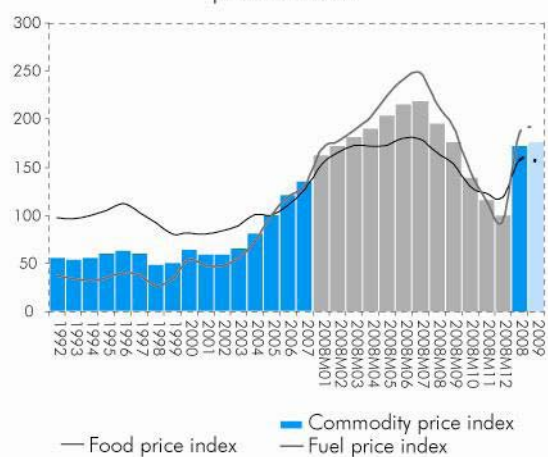
During 2008 basic commodity price index rose on average by 27.6 percent, up from 11.8 percent in 2007. Food and fuel prices rose rapidly, respectively 23.4 and 40.3 percent. The three indices followed

Chart 3 Daily performance of the Euro/USD in international markets



Source: ECB

Chart 4 Raw materials price index performance

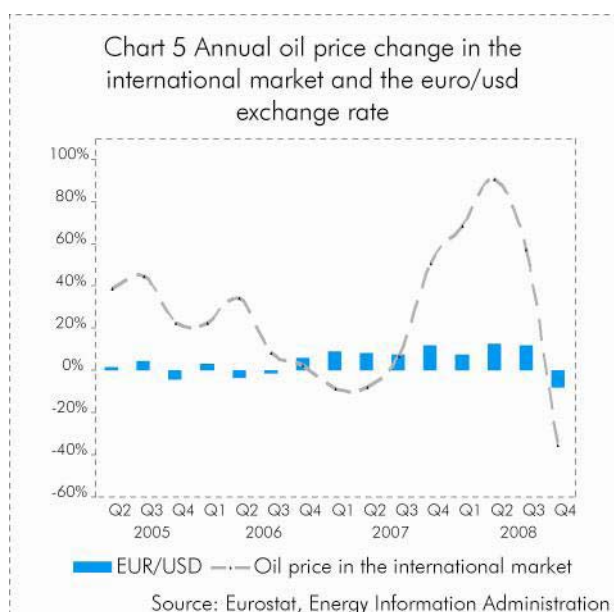


Source: International Monetary Fund

an upswing during the first half of the year, due to reduced supply under the conditions of a relatively high demand. They were downward throughout the second half of 2008, due to contracted demand and the global economic slowdown.

- OIL PRICE

International oil price was highly volatile per barrel. The upward trend that dominated over the first half of the year took the oil price to its highest historical levels. It hit a record in June, when a barrel was traded per about \$134. This was due to the US dollar's depreciation against the main international currencies, rapid raw materials price rise and financial investments concentration in the oil market, under the conditions of the falling value of the main international stock-exchanges¹⁰.



During this period, the oil demand recorded high, though downward values in OECD countries. Due to unfavourable weather conditions and geopolitical turbulence in some of the main oil producing regions, the supply growth decelerated during the same period. July 2008 registered a breaking point of the oil price in the international market. Unfavourable data on economic growth of the OECD countries, the economic slowdown in some of the main emerging economies and appreciation of the US dollar impacted on a rapid oil price drop per barrel.

During the last quarter of the year the price per barrel dropped by on average 50 percent, equalling the 2004 values. Though oil demand growth remained positive in the developed economies, it was insufficient to prevent the demand from contracting, as a consequence of the dampened domestic demand in industrialised countries. Under these conditions, at their meetings in October and November, the OPEC countries agreed to reduce oil production by about 4.2 million barrels, in an effort to reverse the price trend. During 2008 the value per oil barrel increased 38 percent relative to 2007 and this is attributed to January-June price rise.

ENDNOTES

¹ In 2008 the price rise was 10.8 percent for energy and 6.1 percent for the processed food.

² GDP growth for the first half of 2008 averaged 2.3 percent.

³ Average annual inflation rate was 4.0 percent for January-August and 2.1 percent for September–December.

⁴ BRIC countries are Brazil, Russia, India and China.

⁵ In 2007 exports grew by 25.7 percent.

⁶ Consumer spending dropped on average by 0.4 percent during first three quarters of the year, compared to the same period of the previous year.

⁷ Imports fell by 0.2 percent in annual terms, while exports rose by 3.7 percent.

⁸ Inflation rate in September was 4.7 percent, while in December it was 2.2 percent.

⁹ On 8 October 2008 the Federal Reserve, European Central Bank, Bank of Sweden, Bank of England, Bank of Canada, and National Swiss Bank lowered the key interest rate by 0.50 percentage point, in a coordinated unprecedented move. The Central Bank of China dropped its rate by 0.27 percentage point, whereas the Bank of Japan stated that it supported the move.

¹⁰ The US dollar depreciated by about 12 percent against the euro during the first half of 2008, compared to the same period of the previous year.

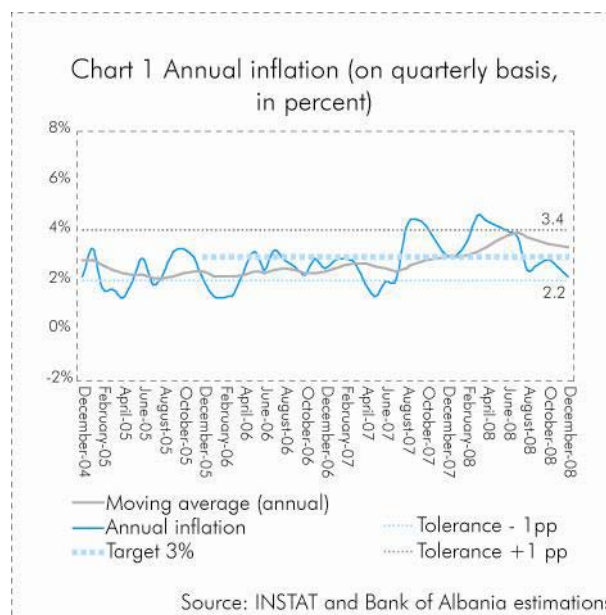
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CHAPTER II THE ALBANIAN ECONOMY

2.1 PRICE STABILITY AND THE BANK OF ALBANIA OBJECTIVE

Notwithstanding the sharp oscillations, the year 2008 witnessed satisfactory consumer price stability. Annual inflation fluctuated within a band of 2.2 to 4.6 percent, remaining within the Bank of Albania tolerance band of 2-4 percent during the major part of the year. Average annual inflation rate for the year 2008 marked 3.4 percent, remaining close to the Bank of Albania 3 percent target¹. Triggered mainly by the rise in primary commodity prices (foods and oil)² in the international markets and the increase in electricity tariffs at home³, average annual inflation marked 3.7 and 4.2 percent over the first and second quarter of 2008. Annual inflation declined over the course of the second half of 2008, owing to the fall of primary commodity prices in the international markets.

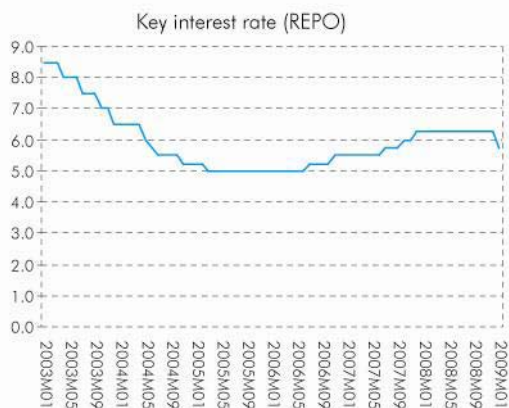
Although upward in the last three years, domestic demand remained contained in 2008. The fall in primary commodity prices in the global markets, reflected in the oil and food prices in the domestic market, the anchored inflation expectations, the contained money growth and the actualization of budget expenditure in line with the projection were conducive to the establishment of an adequate macroeconomic environment to rein in the inflationary pressures. The decline of annual inflation over the second half of 2008 attested to the fact that supply-side shocks in the first half the same year did not yield any second-round effects or trigger the increase of economic agents' inflation expectations.



The Bank of Albania pursued a neutral monetary policy over the course of the year 2008. The key interest rate was kept unchanged at 6.25 percent, which is concurrent with the keeping of inflation within the Bank of Albania objective and the anchoring of inflationary expectations around this objective under a high demand and imported inflation. Additionally, the Bank of Albania took measures to tighten the lending standards, guaranteeing the banks' loan portfolio quality and restraining its high growth rates, which have been fuelling domestic demand over the course of this period.

The last quarter of 2008 witnessed a diverse behaviour of economic indicators. Economic activity and inflationary pressures have been receding

Chart 2 Key interest rate of the Bank of Albania



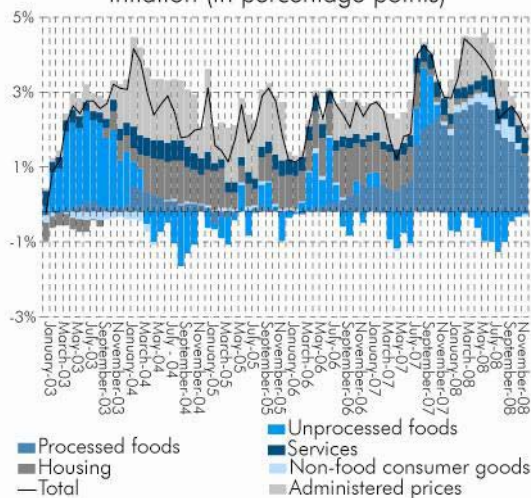
Source: Bank of Albania

triggered by the global financial and economic crisis. Annual inflation rate has been constantly falling to an average of 2.5 percent in the last quarter, which is in line with the Bank of Albania projections. In December, it marked 2.2 percent.

2.1.1 PRICES OF MAIN CONSUMER BASKET ITEMS

The performance of the inflation rate over the course of the year 2008 reflected mainly the effect of the global price rise in primary commodities (foods and fuels). Annual inflation oscillated sharply throughout the year. In the first half of the year, it marked rates above the upper limit of the tolerance band set by the Bank of Albania, reaching 4.6 percent in May, the highest rate in the last five years. The sharp price rise of some primary commodities in the global markets -namely grain and oil- fuelled by the insufficient domestic supply with agricultural products and the energy crisis, gave rise to upward inflationary pressures at home. The increase of electricity tariffs augmented the impact of domestic inflationary pressures over the consumer prices. The extent and the concurrent occurrence of these shocks were reflected in high inflation rates over the first half of the year. In the second half of 2008, annual inflation eased to low rates in all items that fuelled the sharp price rise over August 2007 to June 2008. Subsequently, at end 2008, the inflation rate stood close to the lower limit of the tolerance band. Relative to the first quarter of 2008, average inflation rate for the last quarter was 1.2 percentage points lower.

Chart 3 Contribution of items to annual inflation (in percentage points)



Source: INSTAT and Bank of Albania estimations

The fall in food prices -triggered by the performance of domestic agricultural production and grain prices in the global market- and fuel prices gave rise to the shift in the annual inflation rate trend in the second half of 2008.

Relative to the same period the previous year, the contribution of some goods' and services' items to headline inflation altered notably the extent at which they affected the annual inflation rate over the course of the second half of 2008. In the last quarter, "processed foods" almost reduced their contribution to annual inflation by half relative to February to June the same year. Nonetheless, this item continues to provide the main contribution to total inflation rate, similar to the pre-crisis period in the second half of 2007. From August 2007 to June 2008, this item's contribution to the inflation rate averaged 2.5 percentage points against the average inflation of 3.9 percent

over the same period. In August to December 2008, its contribution reduced to 1.8 percentage points against an average inflation of 2.5 percent. The fall in this item's prices as from August mainly attributed to the dampening strong inflationary pressures deriving from the foreign markets and to the almost complete termination of the bread price rise effects over August 2007 to February 2008.

Annual inflation of "unprocessed foods" marked negative rates throughout the year 2008. This item's inflation dipped by an average of 2.3 percentage points starting from last December. Its rate is mainly affected by the prices of fruit and vegetables, which are highly seasonal and volatile. Prices of fruit and vegetables recorded the sharpest annual fall in May to September 2008, while in the subsequent months they gradually picked up to later peak in December.

	Q3-07	Q4-07	Q1-08	Q2-08	Q3-08	Q4-08
Processed foods (pp)	1.6	2.4	2.5	2.9	2.3	1.7
Bread and cereal (pp)	0.7	1.2	1.4	1.7	1.3	1.0
Alcohol and tobacco (pp)	0.2	0.3	0.1	0.1	0.0	0.1
Unprocessed foods (pp)	0.6	0.5	-0.3	-0.4	-0.9	-0.1
Fruit* (pp)	0.2	0.4	0.5	0.3	-0.1	-0.1
Vegetables*(pp)	0.3	-0.1	-0.9	-0.2	-1.3	-0.7
Services (pp)	0.4	0.4	0.3	0.3	0.5	0.5
Administered prices (pp)	0.4	0.1	0.3	0.7	0.8	0.3
Fuels and energy (pp)	0.2	0.0	0.2	0.6	0.6	0.7
Housing (pp)	0.6	0.2	0.1	0.1	0.0	0.0
Non-food consumer goods	0.0	0.1	0.2	0.3	0.3	0.2
Durable consumer goods (pp)	0.0	-0.1	0.0	0.0	0.0	0.0
Consumer Price Index (y-o-y, %)	3.6	3.6	3.7	4.2	3.0	2.5

Source: INSTAT and Bank of Albania estimations

Table 1 Contribution of items to annual inflation (in percentage points)

Annual inflation rate of "services" marked 4.7 percent, up by 2 percentage points from the average inflation rate in 2007. This item's inflation marked the highest rates in June to October owing to the accumulated price rise of hotel and restaurant services and of transportation services in particular. Prices of hotel and restaurant services rose by an average of 2.5 percent, while as from June, transportation services marked an average annual inflation rate of 20 percent.

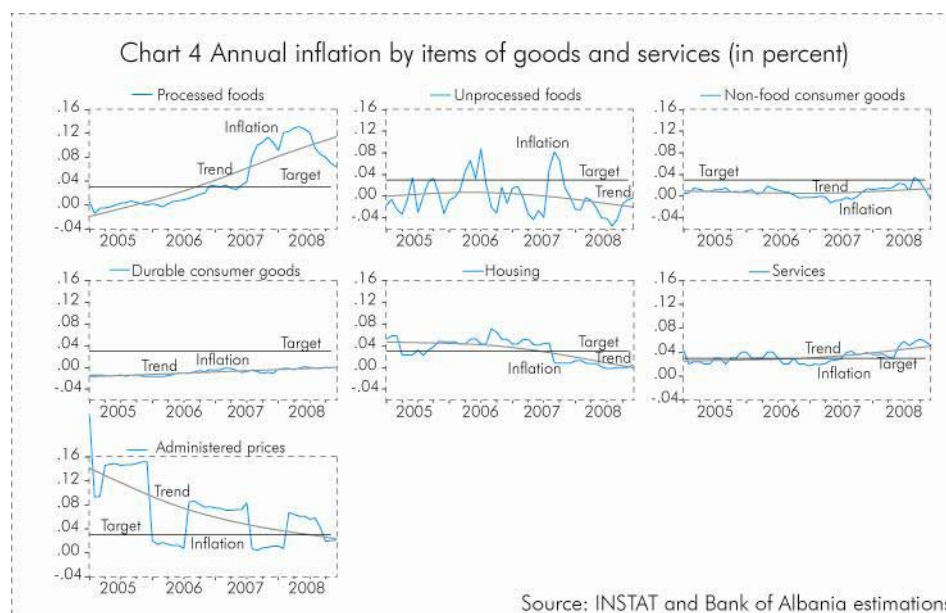
Starting from September 2007, "housing" marked very low inflation rates owing to the stable rent prices. This item's prices rose by an average of 0.5 percent over this period, while in the four preceding years (2003-2007) they rose by an average of 4.3 percent. They remained almost unchanged over the course of the second half of 2008. Rent prices have been persistently affected by the changes in the house market prices, reflecting the situation in this market over the previous year.

Administered prices rose by an average of 4 percent in 2008. This item's annual inflation has been dipping starting from March 2008, shortly after the increase in electricity tariffs. In the second quarter, prices rose by an average

of 6.2 percent to later fall to 2 percent in the last quarter, mainly owing to the lower prices in “communication”⁴.

Prices of “durable consumer goods” dipped over the year 2008. Within this item, “audio-visual equipment” continued to record negative annual inflation rates - 5.5 percent in the second half of 2008.

With respect to “non-food consumer goods”, fuel prices rose sharply in the first eight months to later gradually fall in the subsequent months. In December 2008, the fuel price fell by 7.7 percent. However, the lower fuel price in the domestic market did not record similar rates as in the international market. Along with the negative rate recorded in November, this is the first decrease in the inflation rate of “service to personal vehicles” (wherein oil is part of) after a long period of high inflation starting from mid-2007. Along with the satisfactory situation in food prices and the supply with energy, the year-end 2008 witnessed low domestic inflation pressures.



2.1.2 MAIN INFLATION TRENDS DURING THE YEAR 2008

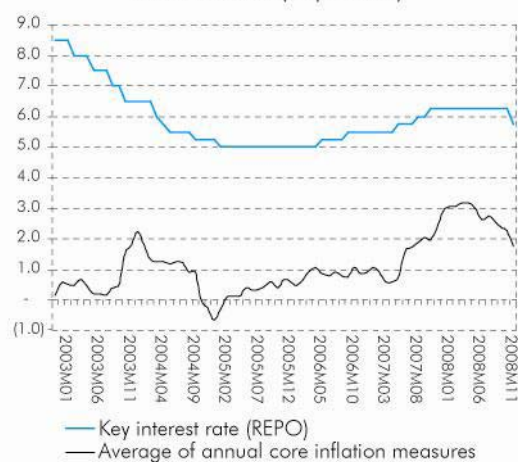
The analysis of consumer price performance for the year 2008 suggests that the high inflationary pressures have reflected both the impact of domestic demand-side pressures and the shocks arising from the performance of commodity prices in the global markets. The high and upward core and non-traded inflation in the first three quarters of 2008 attest to the high domestic demand in economy. Traded and annual non-core inflation were intensely affected by the external sector shocks. The latter are the main factor to have induced oscillating inflation rates over the year.

The year 2008 witnessed relatively high core (long-term) inflation rates. Average year-on-year core inflation measures marked 2.8 percent or 2-3.5

times higher than in the 2006-2007 period. This trend reflected the recurrent upward domestic demand and the tense developments in the performance of primary commodity prices in the foreign markets shown since mid-2006. The same performance was also manifested in the first half of 2008. The relatively long duration and high extent of the high prices in the basic CPI basket products⁵ gave rise to higher core inflation rates, which peaked in May to June 2008. Following this period, it began to gradually descend owing to the lower basic commodity prices in the global markets. Average year-on-year core inflation measures marked 2.6 percent in the second half of 2008. The Bank of Albania's monetary policy also had its say in the decline of core inflation. By pursuing a prudent monetary policy in the last two years, the central bank has helped to rein in the domestic demand pressures in economy. In addition, the stabilization of core inflation rates at around the long-term trend of headline inflation attested to the curbing of inflationary pressures being affected by supply-side factors in the Albanian economy.

In terms of sectoral breakdown of CPI goods and services⁶, it is suggested that the augmented inflationary pressures over the course of the year 2008 have been mainly generated from the external environment. Average traded inflation marked 2.7 percent in 2008, around 2-3 times higher than in the preceding two years. The peak rates were marked in March to June 2008, when traded inflation averaged 3.7 percent. The second half of 2008 witnessed more contained food and primary commodity price rise rates in Albania's main trading partners and in the Euro-zone. This performance was reflected in lower traded inflation rates during the reference period (1.9 percent).

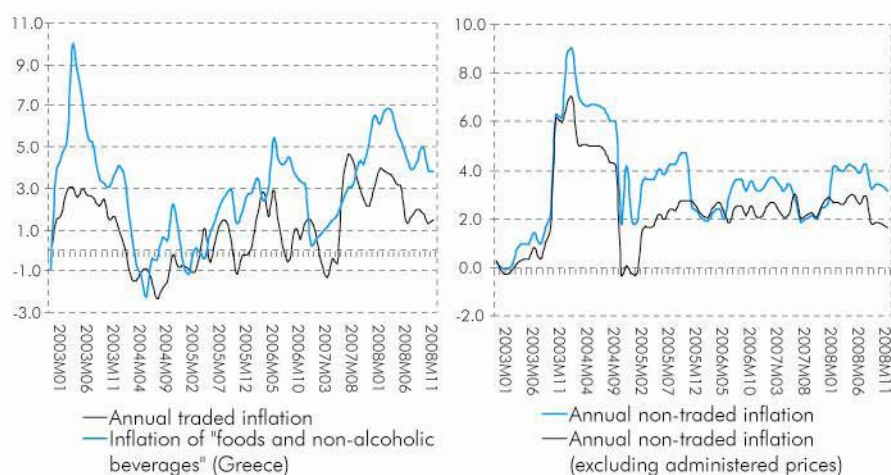
Chart 5 Annual core inflation and key interest rates (in percent)



Source: INSTAT,

Bank of Albania and Bank of Albania estimations

Chart 6 Annual inflation by CPI basket prices (in percent)

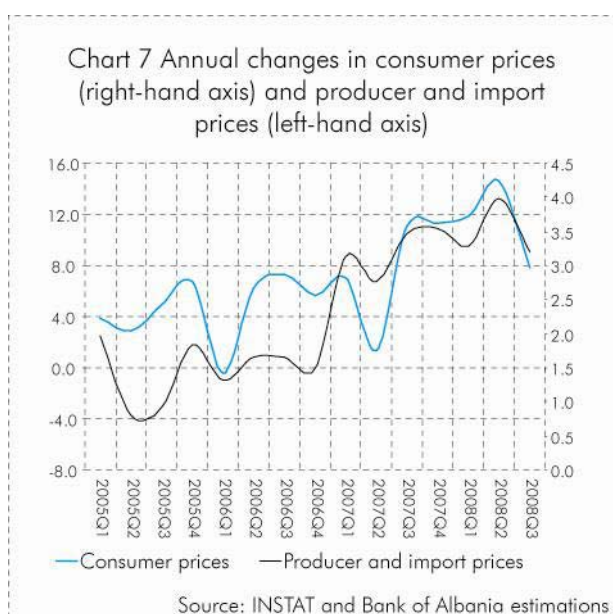


Source: INSTAT, Eurostat and Bank of Albania estimations

The inflationary pressures generated from the domestic demand performance were reflected in the inflation rates of non-traded goods and services. In 2008, non-traded inflation averaged 3.7 percent. The relatively high inflation rates in this sector were also affected by the administrative decisions taken over this year on the increase in some goods and services' tariffs⁷. Excluding the impact of the increase in administrative tariffs, average year-on-year inflation for this sector would have marked around 2.6 percent.

The contained increasing rates of core and non-traded inflation starting from the second half of 2008 attested to the presence of an adequate balance between domestic demand and supply-side factors, which will sustain price stability in the Albanian economy in the medium run.

2.1.3 PRODUCER AND IMPORT PRICES



Producer and import prices were highly affected by the sharp rise in primary commodity prices in the international markets for the major part of the year 2008. The inflationary pressures these prices generated on the overall level of consumer prices were reflected in upward inflation rates in the first half of the year. After reaching the peak rate of the last six years in the second quarter of 2008 (13.3 percent), headline producer and import price index⁸ dropped by 4.2 percentage points in the subsequent quarter. The decline was more pronounced in import prices. The fall in food and oil prices in the global market was reflected in producer and import prices starting from the third quarter of the year 2008.

• PRODUCER PRICES

The Producer Price Index reflects the business costs in production and helps to explain or anticipate the inflationary pressures that may hit the domestic economy. In the first three quarters of 2008, it rose by an average of 7.3 percent, reflecting primarily the higher costs in "food industry" and "food and beverages industry". The accelerated rise in global primary commodity prices exerted upward pressures on the business costs, notwithstanding the stable Albanian Lek vis-à-vis its major currency counterparts⁹. Despite the 32 percent share of these two industries in the PPI basket, their contribution to the annual increase of the Producer Price Index is more than half of the total increase in this index.

Prices of "processed foods" maintained a similar trend to these two industries although at more moderated rates. This behaviour implies that producers have covered a part of producer costs while opting for lower profit margins. Consequently, the higher prices were not passed through to consumers.

Prices in processing industry -the industrial item with the largest share in the PPI basket- rose by an average of 3.7 percent in annual terms. Producer prices in extracting industry increased at accelerated rates in the third quarter of 2008, following the moderate increasing rates starting from the second quarter of 2007.

Table 2 Annual change rates of some PPI and CPI components of "processed foods" (in percent)

	PPI	PPI	PPI	CPI	PPI
		Total processing industry	Food Processing Industry	Processed foods	Extracting industry
Q3:06/Q3:05	0.4	1.2	-2.1	1.1	8.4
Q4:06/Q4:05	-0.7	1.5	1.4	2.4	8.3
Q1:07/Q1:06	2.1	14.4	2.5	3.2	8.1
Q2:07/Q2:06	3.3	7.3	11.3	2.9	2.8
Q3:07/Q3:06	3.6	6.3	14.7	7.3	4.7
Q4:07/Q4:06	7.5	10.2	18.6	10.8	4.5
Q1:08/Q1:07	7.4	6.8	20.5	11.2	5.6
Q2:08/Q2:07	7.4	6.9	14.6	12.9	3.0
Q3:08/Q3:07	7.1	6.1	7.0	10.0	9.7
Q1-3:08/Q1-3:07	7.3	3.7	13.8	11.4	6.1

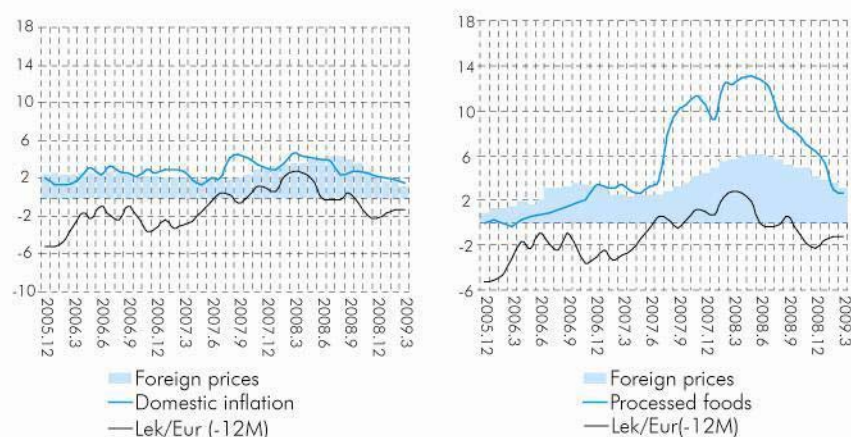
Source: INSTAT

• IMPORT PRICES

Consumer goods' import prices have posted a double-digit year-on-year increase starting from the third quarter of 2007. In the first half of 2008, they increased by an average of 18 percent relative to the historical average of the 2002-2007 period. In the third quarter, import prices of consumer goods fell by 7 percentage points compared with the early part of the year. Inflation at home maintained the same tendency.

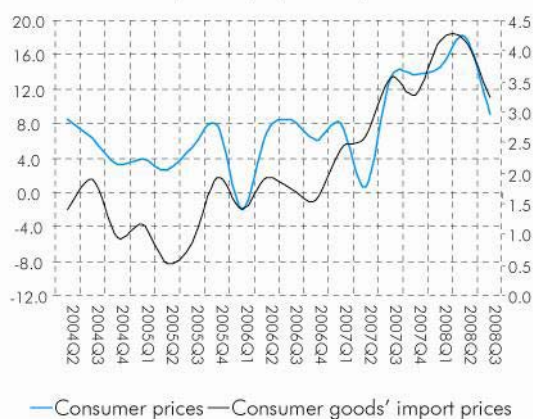
Foreign prices hit the record-high level of 6.1 percent in the second quarter of 2008. In the last two quarters, they rose by slower increasing rates – 5.4 and 4.6 percent, respectively. The downward tendency of foreign prices owed primarily to the lower primary commodity prices (food and oil) and the sluggish economic growth in these countries. In absence of data on

Chart 8 Annual changes in foreign and domestic inflation (left-hand chart) and in foreign and domestic food prices (right-hand chart) and the exchange rate



Source: INSTAT and Bank of Albania estimations

Chart 9 Annual changes in the unit value index for imports of consumer goods and consumer prices (in percent)



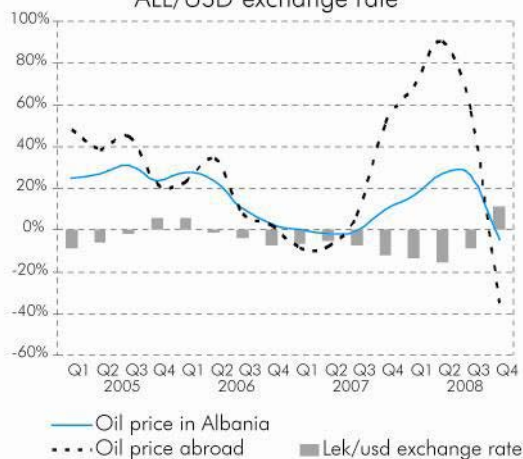
Source: INSTAT and Bank of Albania estimations

the last quarter of 2008, the proxy for imported inflation – measured from food prices¹⁰ in Albania's main trading partners¹¹ – attests to the persistent downward imported inflation for this quarter. The weakened imported inflation rates ascribe to the lower consumer prices in these countries and to the retroactive effect of the appreciation of the Albanian Lek vis-à-vis the Euro over the year.

The performance of consumer goods' (food and clothing) import prices is reflected directly in consumer prices and indirectly in producer prices. The correlation between consumer goods' import prices and consumer prices is found to be statistically significant and immediate.¹²

Average oil price in the domestic market maintained a similar tendency with the oil price in the international market over the course of the year 2008. Retail oil price increased by an average of 15.5 percent relative to the year 2007, with the highest increase in the first three quarters. In December, it fell to the year-end 2005 levels. The period January to August witnessed a constant rise in the oil price per litre in the retail market. The developments in the oil and raw material international market affected the price in the domestic market directly at an average lag of one month. Although the oil price in the international market rose by nearly 38 percent in annual terms, the annual oil price in Albania rose by about 23 percent. The growth rates of the domestic price were more moderate owing mainly to the strong Albanian Lek vis-à-vis the U.S. dollar¹³, which acted as curb on the further upward pressures. Oil price shifted in the last quarter of 2008 when it fell by an average of 14 percent in annual terms. The Albanian Lek began to depreciate against the U.S. dollar and reined in the accelerated fall of the oil price in the retail market.

Chart 10 Oil price annual change in the international and national market and the ALL/USD exchange rate



Source: INSTAT, Bank of Albania, Bloomberg

The CPI basket sub-item "service to personal vehicles" is directly affected by the oil price in the Albanian retail market. In 2008, it increased by an average of 9.2 percent in annual terms. The price performance of this sub-item has reflected the developments in the oil market, falling rapidly in the last quarter. Notwithstanding this sub-item's negligible share in the CPI basket, its contribution to annual inflation for the year 2008 averaged 0.23 percentage points.

2.2. MAIN MACROECONOMIC HIGHLIGHTS

The Albanian economy has by and large featured a positive outlook over the course of the year 2008.

It recorded satisfactory economic growth rates in the first nine-month period and the main macroeconomic stability indicators were maintained. By contrast, the last quarter mirrored quite a diverse outlook of economic developments. Induced by the global financial and economic crisis, the economic activity at home showed signs of slowdown while the monetary indicators have oscillated markedly.

The available data, which mostly cover the first nine-month period, suggest that the economic activity witnessed high growth rates over the year 2008. Turnover volume, a proxy for the value added in economy, increased by an average of 17 percent in the first nine-month period. Taking into account the downturn in the Albanian economic activity in the last quarter, signalled by a range of indirect indicators, namely the deterioration of the economic tendency indicator obtained from the business and consumer opinions on the current and expected economic situation, the decline in remittances and exports in the second half of 2008 and the contracted lending activity in the last quarter, the Bank of Albania considers that the economy has grown in line with the early-year projections.

Economic growth at home has been mainly underpinned by the rapid growth of domestic demand in consumption, investment and government expenditure. It was mainly financed through domestic financial sources and followed by a rapid growth of credit to economy. Notwithstanding the sharp slowdown in the last two months of the year, the banking system's loan portfolio grew by about 35 percent. It has primarily sustained the growth of investment in economy, being manifested in the dominant share of business loans in the loan portfolio. Despite the economic downturn, consumer loans increased substantially as well, attesting to the growth of private consumption in economy.

The high domestic demand and the global economic shocks -materialized in the form of high primary commodity prices- induced high inflation rates in the first half of the year 2008. Average CPI annual inflation marked 3.4 percent for the year 2008, witnessing high rates in the first half of the year. Annual inflation peaked in May at 4.6 percent, the record-high in the last five years. The augmented inflationary pressures gave rise to higher core and non-traded inflation, which also serve as synthetic indicators of inflationary balances in economy. These pressures urged the pursuing of a prudent monetary policy over the year 2008. The key interest rate was kept unchanged throughout the period aiming at better balancing the demand and supply ratios and conducive to the control of inflationary expectations in economy.

The last quarter displayed quite a diverse outlook characterized by sluggish economic activity and higher uncertainty reigning on the financial markets. The deeper global scale financial and economic crisis gave rise to lower primary commodity prices and reduced imported inflation. The relaxation of supply-side shocks and the deceleration in domestic demand in the last quarter induced the progressive decline of the inflation rate to 2.2 percent in December.

In addition, domestic demand prompted the increase in the trade deficit and current account deficit in 2008. The latter accounted for 14.9 percent of the GDP, owing mainly to the rapid growth of imports and decline of remittances in the second half of the year as a result of the deeper economic crisis in the regional peers. On the other side, worth noting is that part of the factors to have led to current account widening, namely the high prices in imported primary commodities and the temporary budget deficit widening as a result of the increase in public investment for the Durrës-Kukës motorway project, are only transitory. In absence of these factors, the current account deficit would have recorded a lower value.

In macroeconomic terms, the widened trade deficit signals higher consumption and investment in economy, which were financed by foreign savings in the form of capital inflows. Foreign currency inflows were sufficient to close the balance of payments in positive terms¹⁴. Making a longer-term analysis, Albania's current account deficit is a natural phenomenon given the country's level of development. Worth noting is that the largest fraction of imports is shared by imports of machinery and appliances and intermediate goods. However, the widened current account deficit requires persistent monitoring. Macroeconomic policies in particular need to be prudent in order to ensure long-term balance of payments sustainability, which is one of the main aspects of macroeconomic stability conditioning long-term economic growth.

Fiscal policy was more expansionary in 2008 reflected in higher public investment and wider budget deficit. Progress in fiscal administration and the country's economic growth within the parameters have allowed higher budget revenues and the control of fiscal deficit at acceptable levels. Public debt increased in 2008 to 55.9 percent of the GDP from 52.8 percent the previous year. However, the improved public debt management in terms of maturity term extension and diversification of financial resources represents a positive development assisting the refinancing of debt and the control of its cost impact on budget indicators.

Table 3 Economic indicators over the years

	2001	2002	2003	2004	2005	2006	2007	2008
Real GDP growth (in %) ¹⁵	7.9	4.2	5.8	5.7	5.7	5.5	6.0*	6.0*
GDP (at current prices, in million ALL ¹⁶)	583,369	622,711	694,098	750,785	814,797	891,000	980,064*	1,064,000*
GDP (at current prices, in million USD) ¹⁷	4,065.3	4,444.8	5,694.0	7,303.4	8,156.1	9,082.6	10,841.4*	12,681.8*
GDP (per capita in USD)	1,323	1,437	1,830	2,336	2,598	2,883	3,429*	3,963*
Number of employed persons (in thousand) ¹⁸	921	920	926	931	932	935	966	970
Unemployment rate	16.4	15.8	15.0	14.4	14.1	13.8	13.5	12.6
Inflation rate (y-o-y at the year-end)	3.5	1.7	3.3	2.2	2.0	2.5	3.1	2.2
Budget deficit (including grants, as a share of GDP) ¹⁹	-6.9	-6.1	-4.9	-5.1	-3.5	-3.3	-3.5	-5.7
Public debt (as a share of GDP)	57.7	62.9	58.9	56.5	57.4	55.5	52.8	55.9
External debt (as a share of GDP) ²⁰	16.3	21.0	18.4	17.2	17.3	16.4	15.1	18.3
Current account (excluding official transfers, as a share of GDP)	-8.2	-10.4	-8.1	-6.9	-9.9	-7.2	-11.1	-15.2
ALL/USD average exchange rate	143.5	140.1	121.9	102.8	99.9	98.1	90.4	83.9
ALL/EUR average exchange rate	129.0	132.4	137.5	127.6	124.2	123.1	123.6	122.8

*Preliminary assessments.

Source: INSTAT, Ministry of Finance, IMF assessments and Bank of Albania, IMF Country Report 09/73, February 2009

Monetary developments have by and large reflected the overall performance of the Albanian economy and the Bank of Albania's monetary policy. Financial intermediation expanded further. Bank deposits to the GDP increased to 80 percent in 2008 relative to 78 percent the previous year. Loans to the GDP increased to 37 percent from 29.7 percent in 2007.

The year 2008 witnessed relatively high money growth rates prompted primarily by the rapid growth of credit to economy. Annual growth rate of M3 averaged 12.3 percent, decelerating slightly from 15.8 percent in 2007. Interest rates in the money market oscillated significantly over the course of the year depending on the performance of liquidity in the system and developments in the international market. In the meantime, the exchange rate remained stable throughout the year.

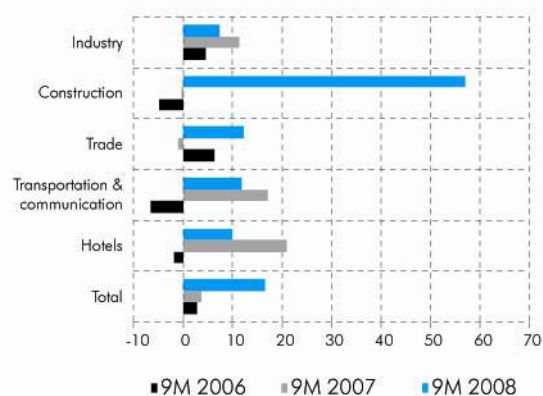
The financial and economic crisis that swept across the world economy in 2008 was dramatic. Its impact over the Albanian economy has been gradually increasing over the last quarter. The uncertainty generated by the turmoil in the global financial system was reflected in the withdrawal of a fraction of deposits from the system in the last quarter of the year. The withdrawals gave rise to liquidity shortages in the system and upward interest rates. On the other side, the system was more reluctant to lend, which in turn led to a marked decline in the lending growth rates over the last quarter. The latter and the decline in remittances caused the economic activity to slow in the last quarter. In response to this situation, the Bank of Albania took measures to inject liquidity and preserve public confidence in the banking system. In addition, it strengthened the supervision regulations aiming at bolstering the financial system's stability. These measures proved effective and the Albanian banking system handled the first shock of global scale financial and economic crisis successfully.

2.2.1 PRODUCTION BY SECTORS OF ECONOMY

Despite the downturn in the last quarter, by and large, the Albanian economy performed well in 2008. Economic activity recorded high growth rates in the first three quarters of 2008. In year-on-year terms, turnover volume growth averaged 17 percent, with the highest growth recorded in the third quarter. Construction and trade recorded the highest annual growth rates. Turnover volume in industry, transportation and communication and hotels declined relative to the previous year.

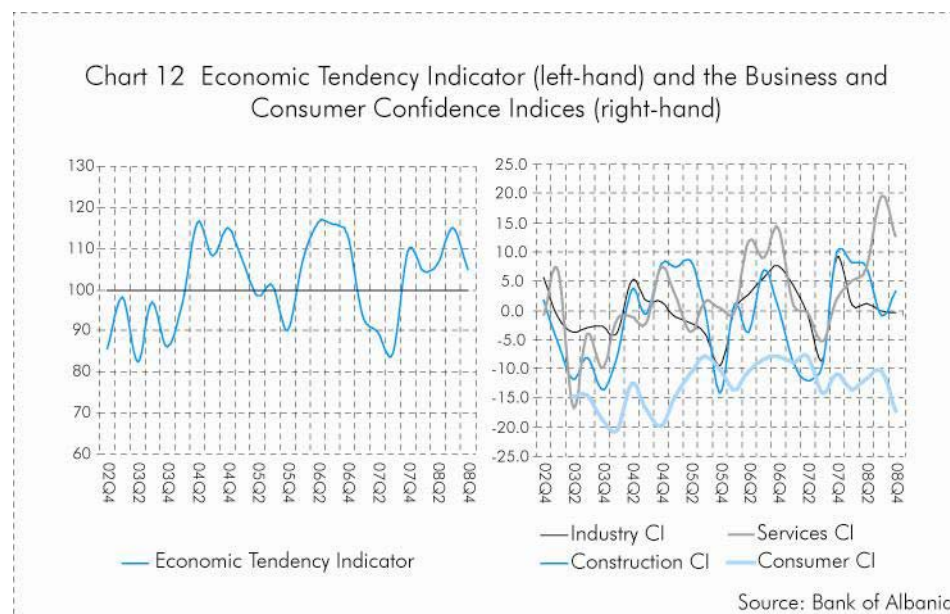
Developments in economic activity over the course of the year 2008 have been also reflected in the performance of the Economic Tendency Indicator (ETI²¹). Following a slight decrease in the first quarter, it increased in the subsequent two

Chart 11 Turnover volume by sectors of economy
(average annual changes of the first three quarters each year, in percent)



Source: INSTAT, Conjunction,
Main Economic Indicators, July-September 2008

quarters to later fall again in the last quarter of 2008²². Business Confidence Indicator by economic sectors attests to its downward tendency in industry and services in the last quarter. By contrast, it improved in the construction sector over the same period. Consumer Confidence Indicator – which has historically recorded negative values – improved in the second and third quarter of 2008. However, it worsened in the last quarter being driven by the deepening of the global scale financial and economic crisis.



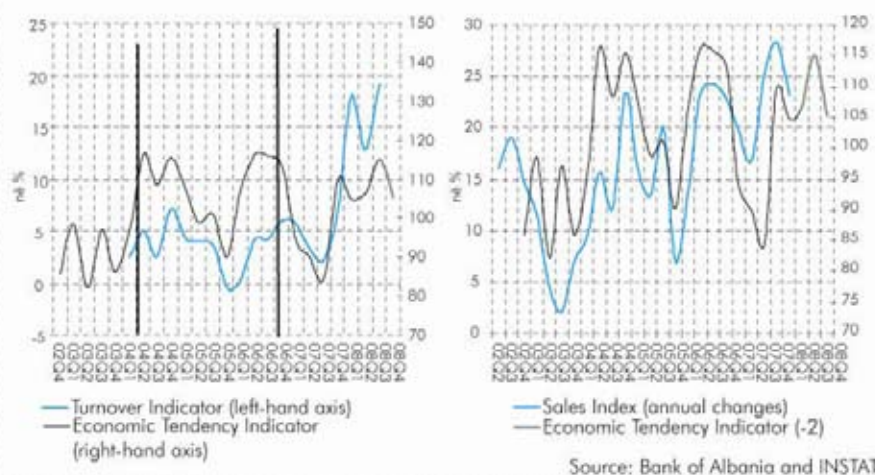
Box 1 Use of Confidence Indices for monitoring the economic developments

Starting from the last quarter of 2008, the Bank of Albania has started to publish the analysis and indicators obtained from the business and consumer confidence indices. The publication of survey results follows a several-year period of studying and testing the obtained indicators. The purpose of the ongoing improvement of questionnaires and the methodologies for building the indicators – on an aggregate basis – is to approximate them with the modern methodologies applied in the central banks of advanced economies.

Confidence indicators used by the Bank of Albania are built based on the information obtained from businesses and consumers in the form of assessments, opinions and expectations. The assessments are collected on quarterly basis via four qualitative questionnaires²³: industry, construction, services and consumers.

The main purpose of confidence indicators is to assist the better understanding of economic agents' behaviour in particular when the course of economic development is vague or close to a turning point in the business cycle. The use of these indicators to describe the economic developments is based on the assumption that the economic agents' confidence accompanies or precedes their decision-making process and behaviour. This implies that the economic agents' judgement and assessment will be reflected in a concrete behaviour and economy-related decision-making. Empirical studies suggest that confidence indicators provide valuable information for explaining

Chart 13 Economic Tendency Indicator and the Sales and Turnover Indicator in total economy (annual changes)



economic behaviours, although at different intensity level in various countries. Consequently, confidence indicators provide important information to the economic decision-making process. By and large, large changes in confidence indicators²⁴ provide signals for current or expected deviation of production from its trend.

In the Albanian case, business and consumer opinions are collected and expressed numerically through balance and confidence indicators. The balance indicator expresses in a simplified way (numerically) the aggregated opinions of respondents in each sector on a given economic phenomenon. The balance indicator is calculated as the difference between positive and negative responses, where the responses are expressed in percentages.

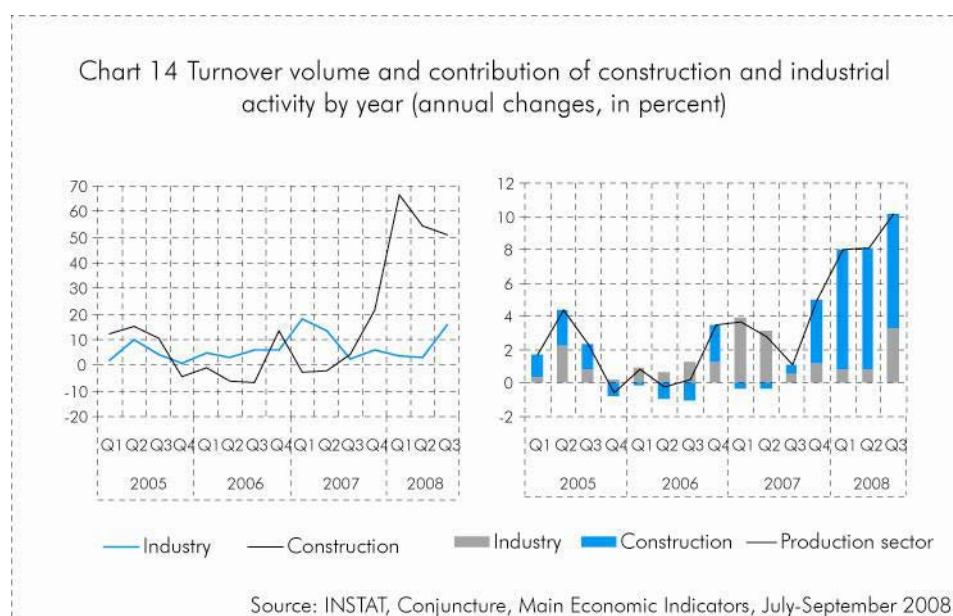
Confidence indicator is built for each sector of the economy and is calculated as the arithmetic average of the main balances' indicators (the selection of balances is based on the statistical characteristics and their economic significance). Economic Tendency Indicator is built based on the confidence indicators for each sector. It expresses the opinions and expectations on the economic activity at home of two of the main economic groups: businesses and consumers.

Starting from the year 2002, confidence indicators at the Bank of Albania have provided a relatively satisfactory insight into the cyclical movements in production, although they are preliminary indicators of developments in various economic areas and do not substitute the official statistics. The testing and improvement of confidence indicators, along with the availability of longer time series from official statistics, aim at better use of information obtained through confidence surveys, in order to monitor the economic developments at home.

- **PRODUCTION SECTOR**

The production sector, which relates to economic activity in construction and industry, posted a significant increase in the first nine months of the year. Growth in the construction sector's economic activity was more rapid than in the production sector's, partly owing to the correction of its slower growth in 2007. The contribution of construction to production has been upward

starting from the third quarter of 2007 and higher relative to industry. As of end the third quarter of 2008, turnover volume in construction recorded higher growth rates compared with industry.



INDUSTRY

Turnover volume in industry grew by an average of 7.4 percent in annual terms in the first three quarters of 2008, which is higher than the annual average of the last four years (5.4 percent). This indicator has increased at comparable rates for processing industry and the supply with energy, gas and water. Processing industry recorded the highest annual growth rate (7.9 percent). By contrast, extracting industry recorded the lowest annual growth rate – 2 from the 6 percent annual change in the last four years.

Table 4 Turnover volume
(average annual changes in
quarters, in percent)

	2004	2005	2006	2007	2008*25
Industry	2.5	4.2	4.9	9.9	7.4
Extracting Industry	-6.0	-9.7	16.8	22.8	2.0
Processing Industry	3.5	5.3	7.4	10.0	7.9
Energy, Gas and Water	2.7	6.4	-6.7	5.1	7.6

Source: INSTAT, Conjuncture, Main Economic Indicators, July-September 2008

PROCESSING INDUSTRY

Turnover volume in processing industry grew by an average of 7.9 percent in the first three quarters of 2008, which is comparable with the preceding two years. "Paper, paperboard and publications industry" (35 percent) and "metallurgy, manufacture of machinery, equipment, electrical and electronic appliances and transportation vehicles" (34 percent) recorded the highest average annual growth rates over this period. By contrast, "manufacture of footwear", "miscellaneous" and "manufacture of textiles" recorded a decline in the turnover volume. "Metallurgy, manufacture of machinery, equipment,

electrical and electronic appliances and transportation vehicles” provided the highest contribution to the annual growth of the turnover volume. Moreover, the manufacture of food products has enhanced its contribution compared with the preceding two years.

PRODUCTION AND CONSUMPTION OF ELECTRICITY

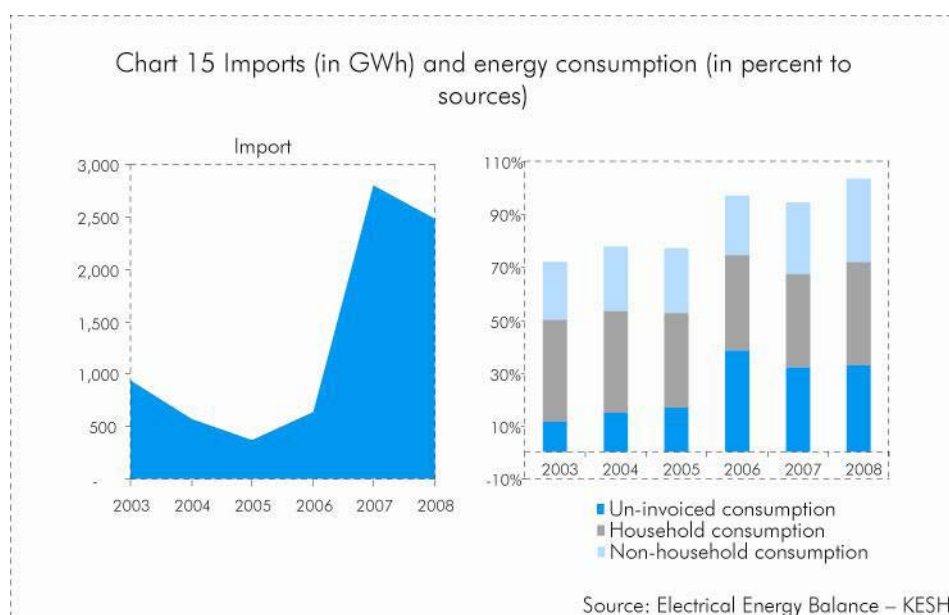
The year 2008 attested to a marked improvement in the main electricity sector’s indicators at home relative to the previous year. The pronounced increase in domestic production due to the favourable hydro meteorological conditions led to fewer imports for this product and lower losses vis-à-vis the produced amount.

	2007	2008	Annual change (in %)
Sources	5,645	6,246	11
Production	2,845	3,771	33
Import (including exchanges)	2,800	2,475	-12
Consumption	5,645	6,246	11
Loss/Production (in percent)	60	46	-14
Energy Consumption	5,514	6,037	9
- Household Consumers	2,078	2,292	10
- Non-Household Consumers	1,563	1,817	16

Source: Electrical Energy Balance – KESH

Table 5 Albanian Electro-Energetic System Balance (in GWh)

The structure of energy consumption for 2008 did not record substantial changes relative to the previous years. According to energy production and consumption statistics, household consumption continues to dominate versus non-household consumption. Including the energy losses in the network, household consumption accounts for around 67 percent of total energy consumed.



Energy losses in the network remain considerable, with direct consequences on the Albanian Electro-Energetic Corporation’s financial situation. In order

to resuscitate the country's ailing electricity sector and improve the energy distribution network, KESH took the first important step for its administrative reformation: the division of the Distribution System Operator (DSO) from the KESH's organizational structure. Another priority in this sector relates to the increase of production capacities at home. Investment in Vlora's TEC and other hydro plants aim at improving the country's energy supply in the future.

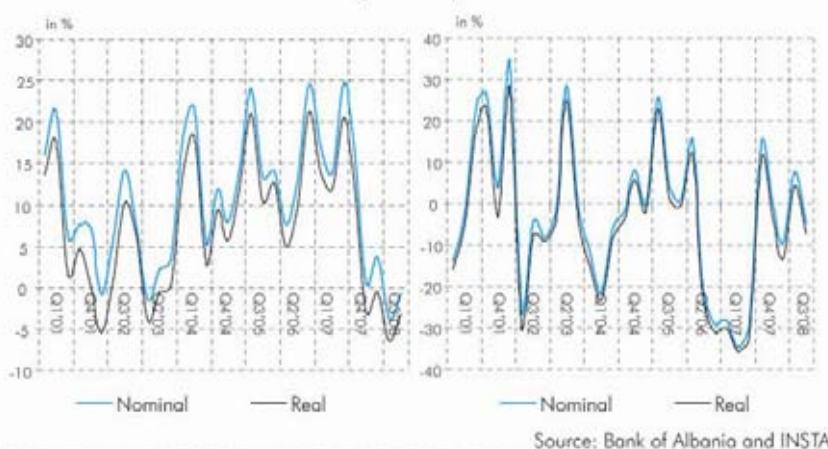
CONSTRUCTION

According to the turnover volume, construction sector recorded an average annual growth of 57 percent in the first nine-month period, with the highest growth in the first quarter to later slightly moderate in the following two quarters. Investment in road infrastructure and the improved level of construction permits have triggered the increase in construction activity. Construction volume for the first three quarters of 2008 recorded an average annual growth of 87 percent with the highest annual growth rate in the second quarter. Preliminary data obtained from surveys suggest a decline in this sector in the following period.

Box 2 Developments in housing market, prices and rents²⁶

The housing market witnessed a moderate growth rate in prices and a volatile rent index over the course of the year 2008. House Price Index posted the lowest annual growth rates since the year 2005. The annual change in this nominal index recorded the lowest rate in the third quarter of 2008 – about -3.7 percent. In real terms²⁷, the change was -6.5 percent. In annual terms, the average House Price Index fell by 0.3 percent in 2008, in contrast to the double-digit growth rates since 2005 (average annual change +16 percent).

Chart 16 Annual change of House Price Index (in nominal and real terms, left-hand) and the annual change of Rent Index (in nominal and real terms, right-hand)

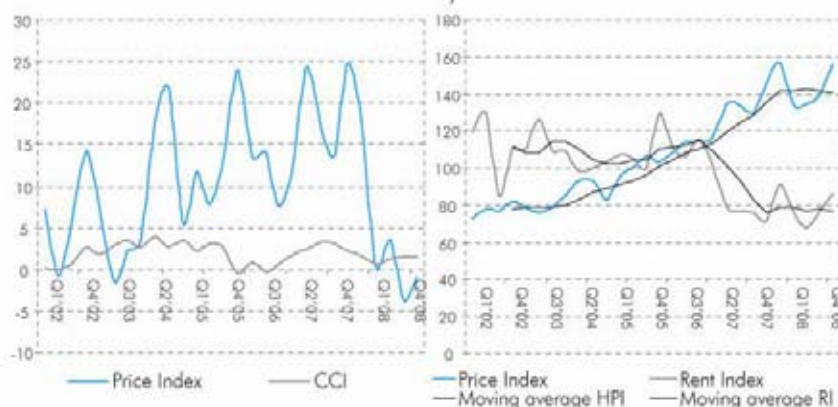


The moderated growth rate in house prices may relate to the lower demand for houses and the relatively upward supply. According to official data, the number of construction permits – often used as an indicator of developments in the construction

sector- has increased suggesting for higher investment in this sector in the following months²⁸. On the other side, the bank lending survey indicated that household demand for house loans had decreased (net balance: -29.3 percent) and the lending standards for this type of loan had tightened (net balance: -52 percent) mainly in the second half of 2008. In the meantime, the Construction Cost Index did not undergo substantial changes in 2008. It also revealed that prices in the house market are mainly driven by other factors different from the construction cost.

The Rent Index manifested higher volatility than the House Price Index and a more distinct downward tendency. Following an annual decrease of 9.5 percent in the second quarter of 2008, the Rent Index increased by 7.5 percent in the third quarter to later fall again in the last quarter by 5 percent. On average, the Rent Index declined by 1.9 percent in 2008 compared with the previous year.

Chart 17 Annual change of the House Price Index and Construction Cost Index (left-hand) and the House Price Index, Rent Index and moving average (right-hand)

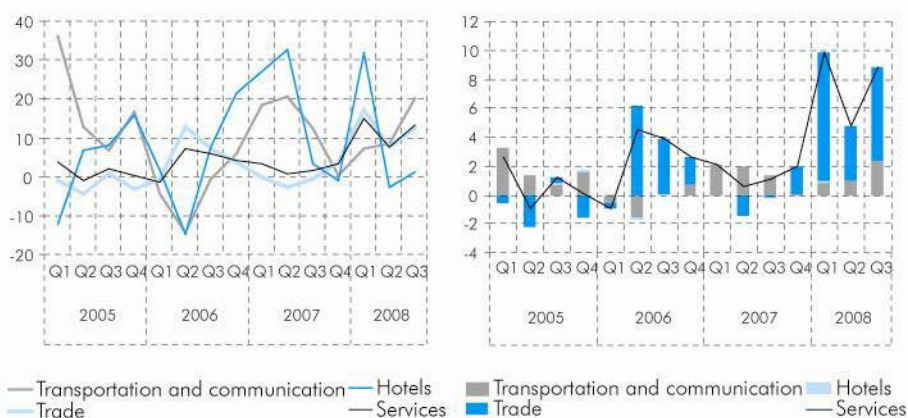


Source: Bank of Albania and INSTAT

• SERVICES

Turnover volume in services posted an average annual growth of 12 percent in the first three quarters of 2008. Trade activity recorded the highest annual

Chart 18 Turnover volume and contribution of branches in services (annual changes, in percent)



Source: INSTAT, Conjuncture, Main Economic Indicators, July-September 2008

growth rate, providing at the same time the highest contribution to the higher annual growth in services.

Trade activity performed satisfactorily in the first three quarters of 2008. "Trade, maintenance and repair of motor vehicles and motorcycles" recorded the highest annual growth rate – around 16 percent. Turnover volume in wholesale and retail trade grew by 11 and 15 percent.

Table 6 Turnover volume by branches of services sector in years (average annual changes of quarters, in percent)

	2004	2005	2006	2007	2008*
Services	5.4	1.3	4.1	2.2	12.1
Trade	9.4	-1.9	5.7	0.2	12.3
Transportation and Communication	-11.7	18.2	-3.4	13.0	11.9
Hotels	13.2	4.5	3.9	15.5	10.0

Source: INSTAT, *Conjuncture, Main Economic Indicators, July-September 2008*

As regards transportation, activity in sea transportation improved in the first three quarters of 2008, while activity in transportation via railways and air transportation recorded slower growth rates in annual terms.

HOTEL ACTIVITY

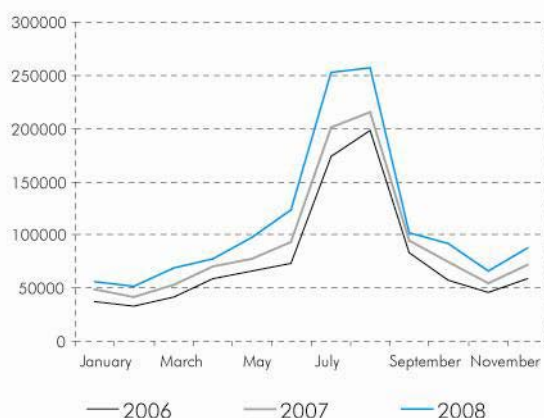
Turnover indicator in hotel activity posted an average annual growth of 10 percent in the first nine-month period. This growth, albeit at double-digit levels, is lower than the average annual growth recorded over the same period the previous year (21 percent). The number of employed persons in hotels increased considerably in the first nine months by 26.1 percent relative to the 7.8 percent increase in the first nine months of 2007. Wages rose by 24.7 percent, which is however lower than the average of the first nine-month period in 2007 (31.9 percent).

Table 7 Hotel activity indicators (annual change, in percent)

	2006	2007	9M -08
Turnover Indicator	3.95	15.5	10
Employed Persons	-2.88	6.25	26.1
Wages	14.2	26	24.7

Source: INSTAT, *Short-Terms Statistics*

Chart 19 Number of foreign travellers during 2006-2008

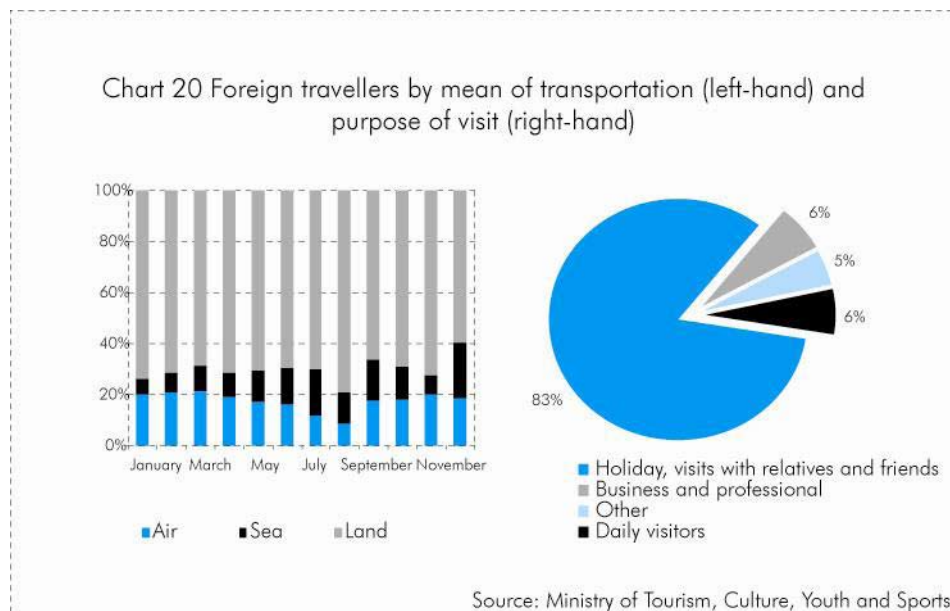


Source: Ministry of Tourism, Culture, Youth and Sports

Around 2.6 million people visited Albania over the course of the year 2008²⁹, out of which 52 percent were foreign travellers³⁰ and 48 percent Albanian ones. The number of foreign travellers increased by 21 percent in 2008. Worth noting is that although around 46 percent of travellers entered Albania in the third quarter of 2008, a considerable number of travellers have also visited Albanian in other quarters³¹. In 2008, the largest number of travellers entered Albania via land (around 70 percent).

In terms of purpose of visit, the largest number of foreign travellers visited Albania for holiday or leisure purposes, visits with relatives and friends while the rest have visited Albania for business, professional, or other services. Travellers from Europe continue

to make up the largest number of foreign travellers (92 percent), followed by U.S. and Asian travellers (5 and 2 percent). Travellers from the regional peers, mainly the Balkan region: Macedonia, Kosovo and Montenegro, make up the largest number of travellers from the European countries.



2.2.2 LABOUR MARKET AND WAGES

• LABOUR MARKET

According to official data available for the first three quarters of 2008, the average number of employed persons has been increasing, while the average number of registered unemployed persons has been declining. Unemployment rate maintained its downward trend with the lowest rate in the third quarter of 2008. The decline is ascribable to the increase in the average number of employed persons in the private agricultural sector, reflecting to a large extent the improved estimation of this indicator.

Labour force and the average number of employed persons increased by 30,585 and 30,527 people, respectively, in the third quarter of 2008. The private agricultural sector provided the main contribution to this increase by 26,549 people. The average number of employed persons in the private non-agricultural sector increased by 4,018 people in the third quarter relative to the preceding one.

	2007				2008			Change in %
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q3 2008 / Q3 2007
Labour Force	1080	1078	1078	1082	1080	1079	1110	3.0
I. Total Employed Persons	933	933	936	939	939	939	970	3.6

Table 8 Employment and unemployment indicators (in thousand people)

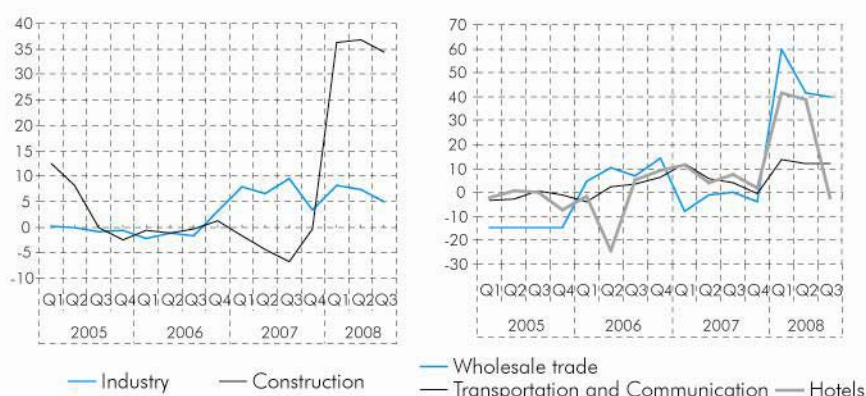
a) In the Public Sector	168	167	167	167	167	167	167	-0.3
b) In the Private Non-Agricultural Sector	223	224	227	230	231	231	235	3.6
c) In the Private Agricultural Sector	542	542	542	542	542	542	569	4.9
II. Unemployed Persons	148	145	142	143	141	140	140	-1.5
Unemployment Rate	13.60	13.50	13.18	13.20	13.04	12.97	12.62	(0.56)*

Source: INSTAT, *Conjuncture, Main Economic Indicators*, July-September 2008

* Change in percentage points.

The year 2008 posted a higher increasing rate in the number of employed persons in non-agricultural economic enterprises relative to the previous year. This reflects the impact of administrative measures for declaring the number of employed persons and the improved economic activity, in particular in construction and trade activity.

Chart 21 The number of employed persons in production and services (annual changes, in percent)



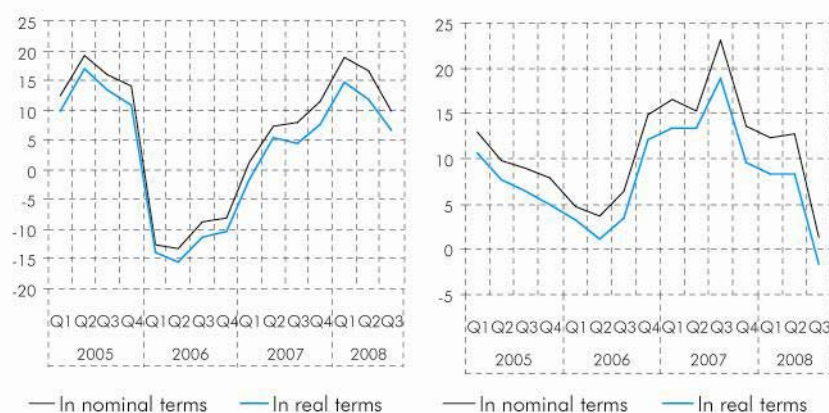
Source: INSTAT, *Short-Term Statistics*, Q3 2008

• WAGES

Annual growth rate of wages decelerated in both the public and the private sector over the course of the first three quarters of 2008. In nominal terms, average monthly wage in the public sector³² rose by 8.8 percent in the first nine-month period³³. Average wage in economic enterprises rose by around 15.1 percent in nominal annual terms³⁴. In real terms, average annual wage rose by 11.0 percent.

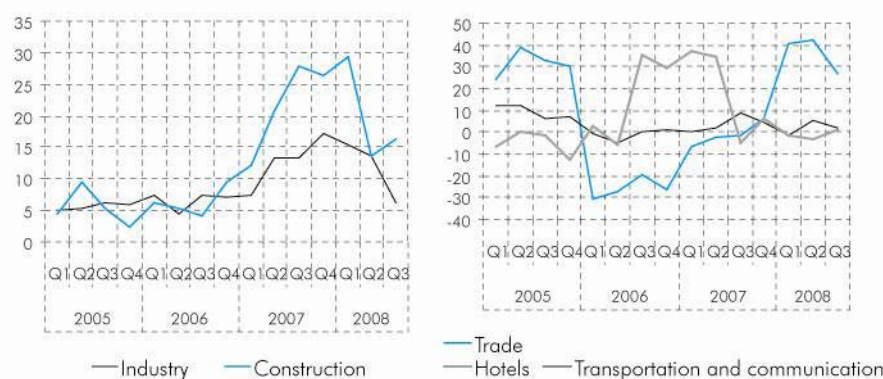
Over the course of the first three quarters of 2008, average annual nominal wage in production sector rose by an average of 19.8 percent in construction and 11.8 percent in industry. In services, wholesale and retail trade posted a high average annual rise by 12.9 and 25.5 percent, respectively.

Chart 22 Average wage in production and services (left-hand) and average monthly wage in the public sector (right-hand) – annual changes, in percent



Source: INSTAT, Conjuncture, Main Economic Indicators, July-September 2008, and Bank of Albania estimations

Chart 23 Average wage in production (left-hand chart) and services (right-hand chart) – annual changes, in percent



Source: INSTAT, Short-term Statistics, Q3 2008, and Bank of Albania estimations

In the third quarter of 2008, monthly base minimum wage stood at ALL 17,000, up by 21.4 percent in annual terms. In 2008, monthly base unemployment benefit stood at ALL 5,980, up by 14.1 percent from the previous year. In annual terms, monthly full economic assistance rose by 37.2 percent to ALL 3,405 in the third quarter of 2008. Monthly partial economic assistance rose by 45.1 percent to ALL 2,518.

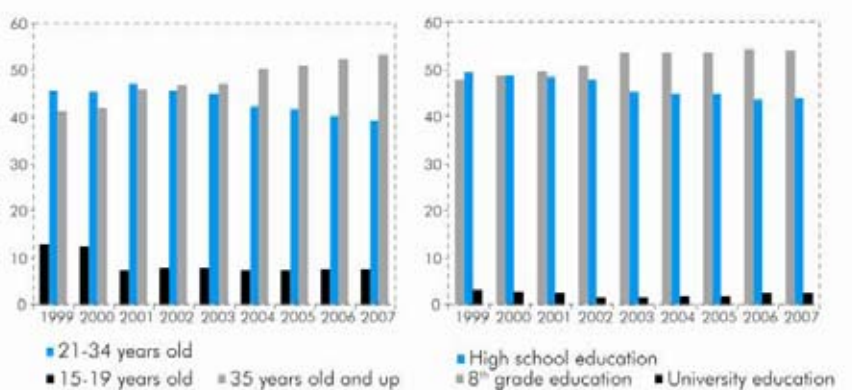
Box 3 Labour market structure in Albania and a comparative approach with the regional countries

Unemployment in general and long-term unemployment in particular bring about manifold negative consequences to emerging countries. In addition to the social-

related issues it generates, the high and stable unemployment rates signal economic structural-related concerns, which may restrain the economic growth rate in the long run. The recent years' positive growth rates in economic activity led to higher employment and lower unemployment rate. In 2007, employment increased to around 56.4 percent from 48.7 percent in 2006. However, it still remains below the Lisbon target of 70 percent. The labour market is highly informal, hence hindering its monitoring through the official data. In addition, the labour market lacks flexibility, which reflects the qualification structure in this market.

According to the Labour Force Survey - 2007, conducted by INSTAT in June 2007, it results that the national employment rate³⁵ among people aged 15 to 64 years is 56.4 percent. The employment rate for youth aged 15 to 24 is low and below the average of other emerging countries, which stands at 40 percent. By contrast, the employment rate for individuals aged 55 to 64 is above the average in other emerging countries – around 30 percent.

Chart 24 The ratio of registered unemployed persons by age to registered unemployed persons (left-hand) and the ratio of unemployed persons by level of education to the registered unemployed persons (right-hand) (in percent)



Source: INSTAT, Employment and Unemployment Indicators

According to the Labour Force Survey, employment is higher and unemployment lower for individuals with higher levels of education. For individuals aged 15 to 64 years, the employment rate for individuals who have completed their eighth grade, high school and university education is 55, 55.8 and 71 percent, respectively.

Table 9 Labour market

	1999	2000	2001	2002	2003	2004	2005	2006	2007
Employment Rate ³⁶ (%)	55.7	55.0	52.1	52.1	51.1	50.3	49.7	48.7	56.4
Employment Rate for Males ³⁷ (%)	69.0	66.0	64.0	63.9	62.6	61.2	60.0	58.8	63.6
Employment Rate for Females ³⁸ (%)	42.3	44.1	39.6	39.7	39.1	38.9	38.8	38.1	49.3
Employment by Main Economic Sectors									
Agriculture (%)	72.1	71.8	57.7	57.7	58.2	58.5	58.5	58.0	47.5
Industry (%)	7.7	5.4	6.0	7.6	7.2	8.1	7.9	8.0	8.8 ³⁹
Construction (%)	1.0	1.2	6.1	6.1	6.0	5.5	5.5	5.7	8.3
Services (%)	19.2	21.5	28.5	28.6	28.5	27.9	28.1	28.3	11 ⁴⁰
Unemployment Rate (%)	18.4	16.8	16.4	15.8	15.0	14.4	14.1	13.8	13.5
Unemployment Rate for Males ⁴¹ (%)	16.4	14.9	14.2	13.6	12.9	12.4	12.1	11.8	14.4
Unemployment Rate for Females ⁴² (%)	21.4	19.3	19.9	19.1	18.2	17.5	17.2	16.8	12.2

Source: INSTAT, Social Indicators, Employment, Unemployment, "Albania 2008 Progress Report" EU

Unemployment rate for the period when the survey was conducted is 13.5 percent, while the unemployment rate for individuals aged 55 to 64 exceeds this figure. Long-term unemployment for 2007 accounts for around 86.8 percent of registered unemployed persons⁴³. According to data made available by the INSTAT, unemployment for individuals aged 15 to 19 and 21 to 34 accounts for 7 and 39 percent of registered unemployed persons.

Table 10 Unemployment rate in Albania and regional countries

Unemployment Rate (in %)	2005	2006	2007	2008		
				Q1	Q2	Q3
Croatia			9.6	14.7	13.2	12.4
Macedonia	37.3	36	34.9	34.8	33.8	33.0
Turkey	10.2	9.9	9.9	11.6	8.9	9.8
Albania	14.3	13.9	13.4	13.04	12.97	12.62
Bosnia and Herzegovina	44.7	44.2	42.9	39.9	41.0	40.5
Montenegro	18.5	14.7	11.9	11.8	11	10.7
Serbia	21.8	21.6	18.8	17.1	13	12.5

Source: "EU Candidate and Pre-Accession Countries Economic Quarterly", EU, 8 October 2008, 9 January 2009

2.3 BALANCE OF PAYMENTS

The external sector of economy witnessed further deepening of the current account deficit in 2008 to 14.9 percent of GDP from 10.4 percent the previous year. The widened current deficit suggests for added activity in the external sector of the economy and in imports particularly. Notwithstanding the higher exports, trade deficit -which provides the main contribution to current deficit widening- has been going up. Remittances, which were down by 16 percent in 2008, have financed around 33 percent of the trade deficit. The year 2008 witnessed considerable increase in net foreign direct investment (32 percent). Their relative indicator as a share of GDP accounts for 7.2 percent compared to 5.9 percent the previous year.

	In millions of euros			As a share of GDP		
	2006	2007	2008	2006	2007	2008
Current Account	-471.0	-831.0	-1,290.6	-6.5	-10.4	-14.9
Trade Balance	-1,658.9	-2,104.0	-2,415.5	-22.9	-26.6	-27.9
- Exports	630.6	786.3	915.9	8.7	9.9	10.6
- Imports	-2,289.6	-2,890.4	-3,331.4	-31.6	-36.5	-38.4
Services (net)	-31.5	12.9	-14.7	-0.4	0.2	-0.2
Revenues (net)	208.8	217.3	309.4	2.9	2.7	3.6
Current Transfers (net)	1,010.6	1,042.9	830.1	14.0	13.2	9.6
Capital and financial account	558.4	848.4	1,555.7	7.7	10.7	18.0
Overall balance	206.6	148.6	191.9	2.9	1.9	2.2

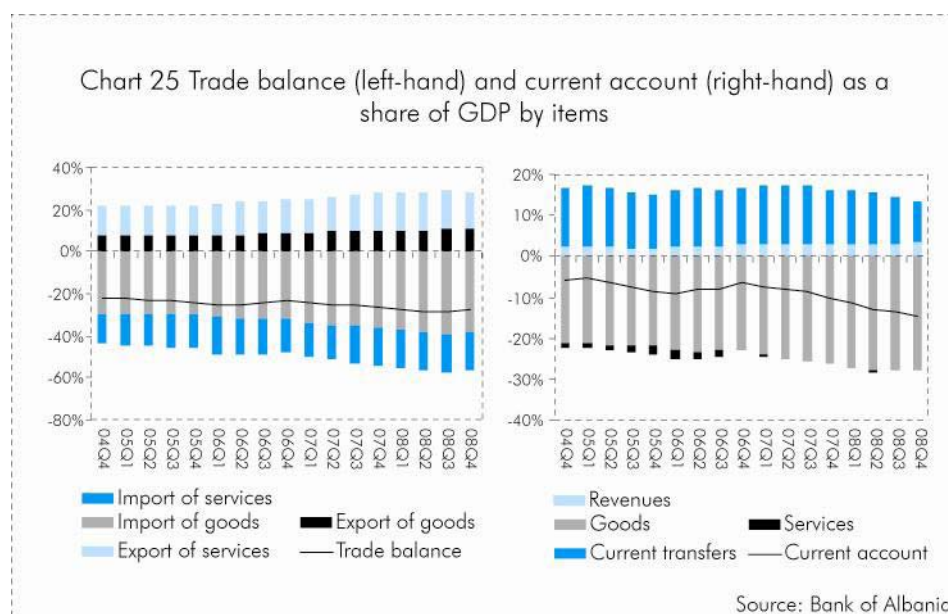
Source: Bank of Albania

Table 11 Balance of Payments indicators in years

CURRENT ACCOUNT

The year 2008 witnessed intensive activity in the external sector of the economy expressed in the increase of current expenditure and revenue⁴⁴.

Current transactions' volume grew by 12 percent and amounted to EUR 9.2 billion. Out of this figure, 62 percent were used for expenditure. Around 93 percent of current expenditure were for purchases of goods and services. The main sources of revenues were the exports of goods and services (62 percent), current transfers (26 percent) and labour and investment income (12 percent).



TRADE IN GOODS

The large flow of trade exchanges resulted in a total trading volume of EUR 4.2 billion, up by 16 percent from the previous year. The contribution of trade in goods to current account remains high, accounting for 46 percent of all current transactions.

Table 12 External trade

	Imports (%)		Exports (%)		'08/'07 (%)	
	2007	2008	2007	2008	Imports	Exports
Food and Live Animals	12.5	11.9	3.6	3.5	11.4	13.5
Beverages and Tobacco	2.9	3.2	1.4	0.3	26.4	-76.2
Unprocessed Materials	2.2	2.1	9.6	11.8	9.1	42.5
Fuels	14.7	15.9	7.9	8.9	26.4	30.4
Animal of Vegetable Fats and Oils	1.1	1.5	0.1	0.0	52.8	-70.7
Products of Chemical Industry	9.9	9.7	1.0	1.1	14.6	26.0
Processed Goods	24.8	23.9	21.3	25.3	12.4	38.5
Machinery and Appliances	20.7	22.0	4.2	4.1	23.8	14.8
Other Processed Foods	11.2	9.9	50.8	44.9	4.2	3.0
Goods, not elsewhere classified	0.0	0.0	0.0	0.0	0.0	0.0
Total	100.0	100.0	100.0	100.0	15.3	16.5

Source: Bank of Albania

Trade dynamics attests to high upward rates over the course of the year 2008 both in imports (15.3 percent) and exports (16.5 percent). However, the annual growth rate of exports and imports was lower relative to the previous

year⁴⁵. Despite the almost comparable growth rates of imports and exports, the low base of the latter caused the trade deficit to deepen further. In 2008 it amounted to EUR 2.4 billion, up by 14.8 percent from the previous year. The insufficient production capacities at home to meet the growing demand of the Albanian economy for goods led the coverage ratio of imports from exports to remain low at around 27 percent. The latter have not undergone significant changes over the last three years.

The Albanian imports by final use attest to a pronounced concentration of intermediate goods (56 percent), while capital and consumer goods account for 29 and 15 percent of total imports. Processed industrial goods account for 57 percent of intermediate goods. The share of consumer goods' imports declined by 6 percentage points in annual terms, while capital goods recorded the highest increase by 29 percent.

Table 13 External trade by trading partners

	Share to total imports		2008/2007 (in %)	Share to total exports		2008/2007 (in %)
	2007	2008		2007	2008	
EU countries - 15, of which:	54.1	54.2	16.9	81.8	78.0	11.2
Italy	27.2	26.6	14.3	68.0	61.8	5.8
Greece	14.6	14.7	17.7	8.3	8.8	23.5
Germany	5.5	6.1	29.2	2.4	2.7	27.8
New EU Member States, of which:	5.7	6.7	37.7	1.3	1.6	45.7
Bulgaria	1.8	1.9	26.1	0.7	0.7	21.3
Czech Republic	0.8	0.8	19.0	0.0	0.1	83.7
Romania	0.4	0.5	48.3	0.3	0.2	-37.7
Other European countries, of which:	11.6	11.6	-12.6	0.3	2.2	662.4
Russia	4.1	4.4	24.8	0.3	1.1	388.2
Ukraine	2.6	1.5	-34.2	0.0	0.0	997.0
The Balkans	13.2	13.7	4.5	12.1	15.2	34.6
Bosnia and Herzegovina	0.3	0.3	12.3	0.4	0.2	-51.5
Croatia	0.9	1.0	19.8	4.8	0.2	111.5
Kosovo	0.6	0.6	20.7	0.1	6.6	60.3
Macedonia	1.9	2.2	33.4	2.4	2.9	45.9
Serbia	2.2	0.0	-97.8	1.8	0.1	-96.3
Montenegro	0.1	0.2	133.0	0.4	2.1	443.2
Turkey	7.3	6.0	-3.6	2.2	1.9	-1.4
USA	2.5	1.1	24.2	0.7	0.4	-32.5
Asia, of which:	7.6	9.0	33.2	2.6	2.8	25.8
China	6.7	7.5	30.9	2.6	2.8	26.4
Total	100.0	100.0	15.3	100.0	100.0	16.5

Source: Bank of Albania

With respect to exports, they increased in all commodity groups. The Albanian exports remain highly reliant on textiles and footwear industry, accounting for 43.4 percent of total exports. Exports of mineral products (8 times higher than in 2007) and fuels (30 percent) grew sharply in 2008. By contrast, exports of beverages and tobacco recorded a substantial decline (76.2 percent).

As in the previous year, Kosovo's market absorbs the major fraction of our exports with the region, being also the sole country we have trade surplus with. Other trading partners consolidating in the Albanian market include Germany and Russia.

SERVICES

Services' transactions increased by 9 percent in annual terms to 35 percent of the GDP. Services' account balance ended negative with around EUR 15 million. The surplus in revenue from "travel services" and "other services" did not manage to offset the deficit in "transportation expenditure" and "insurance expenditure".

Trade in services seems to be quite dynamic, particularly exports, which continue to outdo exports of goods by as much as 1.7 times. Travel services -mainly for personal purposes- make up the largest item in both exported and imported services sharing 78 and 68 percent, respectively. Worth noting is the boom in foreign currency inflows from tourism export, which amounted to EUR 1.2 billion⁴⁶ - sharply higher than the export of goods. Simultaneously, Albanian travellers' demand for goods and services in other foreign countries pushed imported travel services to amount to around EUR 1 billion. This type of expenditure is estimated to have increased by 14 percent relative to the previous year.

Albania remains a net importing country of transportation and insurance services owing to the higher import of goods. "Other services" ended in a surplus of around EUR 54 million with communication, governmental and construction services providing the main contribution. Financial services recorded a negative figure of around EUR 2 million.

REVENUES AND CURRENT TRANSFERS

As of end 2008, the positive income balance (EUR 309 million) is estimated to have increased by more than 40 percent relative to the previous year. Portfolio investment income provided the main contribution. Over the course of the year 2008, Albania paid off EUR 28 million on foreign debt interests, which have increased relative to 2007⁴⁷.

Total remittances for 2008 are estimated to be EUR 800 million (down by 16 percent in annual terms) or 9.2 percent of GDP. The economic and financial crisis in the countries with the highest number of Albanian emigrants is believed to have pushed the workers' remittances down. Remittances have contributed by 33 percent to the reduction of the trade deficit – down by 12 percentage points relative to the previous year. Official transfers are estimated at about EUR 27 million, downward compared with the previous year.

CAPITAL AND FINANCIAL ACCOUNT

Considerable capital flows moved both ways in 2008, as income and outgoing flows. The net flow in capital and financial account yielded a positive figure of around EUR 1.56 billion or twice as much higher than in 2007. 83 percent of the current account deficit is covered by the positive capital and financial account balance, which accounts for 18 percent of the GDP. Around EUR 78 million entered the country in the form of capital transfers and 1.38 billion in the form of residents' financial liabilities.

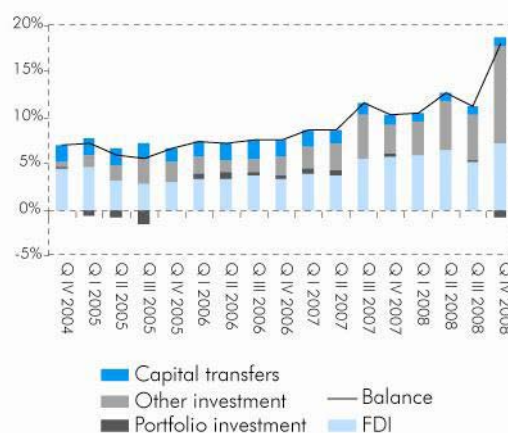
Foreign direct investment (inflows) hit a record level in 2008, bringing in EUR 680 million or 42 percent higher than in 2007. Net foreign direct

investment as a share of GDP accounts for 7.2 percent, up by 1.2 percentage points compared to the previous year.

External debt service for 2008 accounts for 11 percent of our exports in 2008, providing evidence for satisfactory levels of solvency. Foreign currency assets invested abroad dropped by around EUR 93.8 million. Worth noting are non-residents' financial liabilities, in the form of lower residents' financial assets⁴⁸, which amounted to EUR 225 million.

The overall balance of payments position is positive, yielding a growth of EUR 191.9 million in the foreign reserves held by the monetary authority. As a result, their level at end 2008 reached EUR 1.69 billion, sufficient enough to cover 4.2 months of imports of goods and services.

Chart 26 Capital and financial account as a share of GDP by items



Source: Bank of Albania

2.4 FISCAL POLICY AND THE MAIN FISCAL INDICATORS⁴⁹

Fiscal policy was more expansionary in 2008 reflected in higher public expenditure and wider budget deficit. Budget revenues and expenditure increased by 15.3 and 22.6 percent, respectively, accounting for 27.3 and 32.9 percent of GDP. Budget deficit deepened by 2.2 percentage points in annual terms, accounting for 5.7 percent of GDP. Investment expenditure -mainly on Durrës-Kukës motorway- provided the main contribution to the further deepening of fiscal deficit. In annual terms, capital expenditure rose by 2.8 percentage points as a share of GDP. The expansionary fiscal policy has provided a fiscal drive to the economy.

	2005	2006	2007	2008
Total Revenue	25.06	25.75	25.70	27.26
i. Grants	0.76	0.90	0.13	0.29
ii. Tax and Customs Duties	16.64	17.41	18.06	19.28
- VAT	7.92	8.34	8.97	10.07
- Profit Tax	2.36	2.50	2.15	1.70
- Excise Tax	2.27	2.58	2.93	3.06
- Personal Income Tax	0.91	0.96	1.52	2.29
iii. Local Government	1.48	1.25	0.96	1.06
iv. Contributions	4.44	4.41	4.29	4.47
v. Non-Tax Revenue	1.74	1.78	2.26	2.16
Total Expenditure	28.51	29.05	29.18	32.92
i. Current Expenditure	23.81	22.99	22.98	23.54
- Personnel Cost	6.59	6.36	6.04	6.26
- Interest	3.19	2.81	2.61	2.94
- Operations	3.01	2.56	2.58	2.72
- Subsidies	0.45	0.43	0.36	0.24
- Social Insurance Outlays	6.86	6.74	7.14	7.16
- Local Government Expenditure	2.45	2.55	2.18	2.55

Table 14 Fiscal indicators as a share of GDP (in percent), 2005-2008

- Social Protection Transfers	1.25	1.55	1.51	1.67
ii. Capital Expenditure	4.71	5.74	5.83	8.68
iii. Capital Transfer to KESH	-	-	0.35	0.24
iv. Additional Capital Spending	-	0.32	0.07	0.46
Cash Balance	- 3.46	- 3.30	- 3.49	- 5.66
- Domestic Financing	2.86	2.65	2.94	2.31
- Foreign Financing	0.60	0.65	0.54	3.35

Source: Ministry of Finance, INSTAT, IMF Country Report 09/73, February 2009

Notwithstanding the high growth rates, budget revenues and expenditures did not meet the annual projection of the Ministry of Finance⁵⁰. Referring to the budget projection revised in December 2008⁵¹, budget revenues and expenditure were met by 97.3 and 98.7 percent of the projected target. Both figures are higher than in the previous years.

Table 15 Projected and estimated budget indicators for 2008

	Estimation	Projection 2008 (in billions of leks)			Projection 2008 (as a share of GDP)		
	2008	Initial	Revised	Normative Act	Initial	Revised	Normative Act
Total Revenue	290.08	283.69	303.78	298.22	26.66	28.55	28.03
i. Grants	3.05	4.73	4.67	2.51	0.44	0.44	0.24
ii. Tax and Customs Duties	205.18	195.71	209.71	209.71	18.39	19.71	19.71
- VAT	107.09	99.90	104.90	106.90	9.39	9.86	10.05
- Profit Tax	18.11	14.42	18.42	18.42	1.36	1.73	1.73
- Excise Tax	32.51	38.49	37.49	35.49	3.62	3.52	3.34
- Personal Income Tax	24.38	16.27	23.27	23.27	1.53	2.19	2.19
iii. Local Government	11.31	15.58	15.58	13.08	1.46	1.46	1.23
iv. Contributions	47.59	51.06	51.06	48.16	4.80	4.80	4.53
v. Non-Tax Revenue	22.95	16.60	22.76	24.76	1.56	2.14	2.33
Total Expenditure	350.27	369.03	360.21	354.76	34.68	33.85	33.34
i. Current Expenditure	250.49	253.05	257.41	254.84	23.78	24.19	23.95
- Personnel Cost	66.62	67.96	67.96	67.06	6.39	6.39	6.30
- Interest	31.31	33.28	32.58	31.58	3.13	3.06	2.97
- Operations	28.96	28.02	28.64	28.08	2.63	2.69	2.64
- Subsidies	2.55	2.28	1.97	2.57	0.21	0.18	0.24
- Social Insurance Outlays	76.21	76.00	78.67	77.87	7.14	7.39	7.32
- Local Government Expenditure	27.12	29.57	31.65	29.15	2.78	2.97	2.74
- Social Protection Transfers	17.73	15.94	15.94	18.54	1.50	1.50	1.74
ii. Capital Expenditure	92.37	105.58	94.42	91.14	9.92	8.87	8.57
iii. Capital Transfer to KESH	2.52	-	0.48	0.48	-	0.05	0.05
iv. Reserve Funds	-	10.40	9.90	5.70	0.98	0.93	0.54
Cash Balance	- 60.19	- 85.35	- 56.42	- 56.54	- 8.02	- 5.30	- 5.31
- Domestic Financing	24.53	29.42	21.10	21.85	2.76	1.98	2.05
- Foreign Financing	35.66	55.93	35.33	34.69	5.26	3.32	3.26

GDP for 2008 (in billions of leks): 1,064 (IMF Country Report 09/73, February 2009)

Source: Ministry of Finance

With respect to quarterly distribution, revenues have been quite uniform over the quarters, while budget expenditures were mainly concentrated in the second and last quarter of the year. The high concentration of expenditure -in particular in the last months of the year as in the previous two years- has exerted upward pressures on the interest rates in the Government securities' market.

In structural terms, public finances were more oriented to achieving the objectives and priorities established in the National Strategy for Development and Integration⁵². Similarly to the previous years, the basic challenges and

priorities related to fiscal policy entail:

- The achievement and maintenance of macroeconomic stability;
- The improvement in the management of public finance, public debt, revenue collection system and the improvement of the business climate;
- The further fiscal consolidation (reduction of the public debt ratio to the GDP);
- The enlargement of the tax base and the harmonization of tax policies with the country's development priorities.

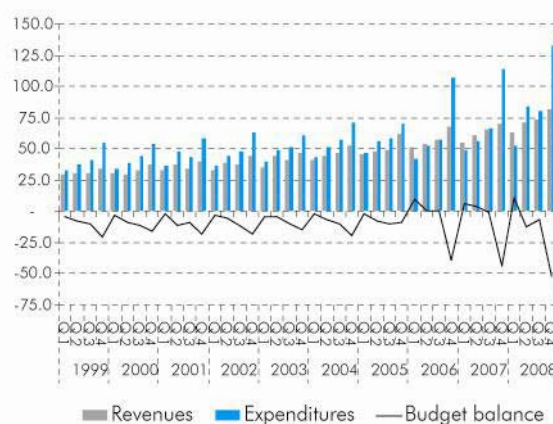
Broadly speaking, numerous positive steps have been taken with respect to meeting the main objectives, some of which part of the PRGF/EFF arrangement with the IMF. If we refer to the meeting level of the structural benchmarks established in this arrangement, the 2008 developments are by and large satisfactory⁵³.

• BUDGET REVENUES

Budget revenues increased by 15.3 percent in 2008 and accounted for 27.3 percent of GDP. The country's economic growth and the improved management of the revenue collection system provided a positive impact over the increase of revenues. Total revenues as a share of GDP increased by about 1.6 percentage points in 2008.

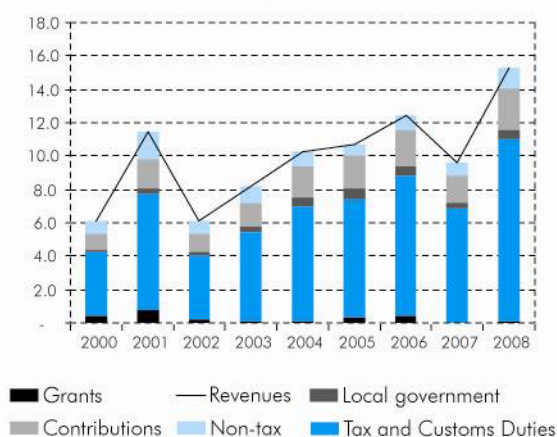
Tax and customs duties continue to provide the highest contribution to the increase in total revenues. Their share to the total accounts for about 70 percent.

Chart 27 Main fiscal indicators by quarters, Q1 1999-Q4 2008



Source: Ministry of Finance

Chart 28 Annual nominal change of revenues by main items, 2000 – 2008



Source: Ministry of Finance and Bank of Albania estimations

Table 16 Budget revenues by main items

In billions of leks	Average 2005-2007	2007	2008				Total
			Q1	Q2	Q3	Q4	
Total Revenue	228.39	251.56	63.59	71.40	73.93	81.16	290.08
i. Grants	5.16	1.28	0.04	0.48	0.20	2.33	3.05
ii. Tax and Customs Duties	155.84	176.81	46.87	49.23	53.85	55.24	205.18
- VAT	75.52	87.77	24.02	25.72	28.25	29.10	107.09
- Profit Tax	20.86	21.08	6.05	3.79	3.64	4.63	18.11
- Excise Tax	23.42	28.73	6.52	8.42	9.94	7.63	32.51
- Personal Income Tax	10.28	14.85	4.82	5.18	6.26	8.13	24.38
- National Taxes	13.27	14.53	3.40	3.91	3.68	3.43	14.42
- Customs Duties	12.49	9.85	2.06	2.21	2.08	2.32	8.66
iii. Local Government	10.83	9.37	2.42	3.04	2.94	2.91	11.31
iv. Independent Budget	39.16	41.99	11.13	11.31	11.83	13.32	47.59
v. Non-Tax	17.40	22.11	3.13	7.34	5.11	7.37	22.95

Source: Ministry of Finance

Revenues from VAT share the main weight in total revenues – approximately 37 percent. Although the VAT rate did not undergo any changes compared with the previous year, this type of revenue has increased its contribution to total revenues for 2008 pronouncedly. The reduced legal relief for the VAT until mid-2007 is one of the main factors to have provided a positive contribution to this growth.

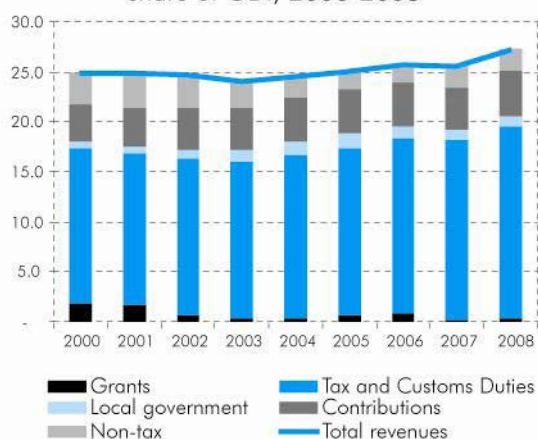
Despite the global markets' developments over the course of the second half of 2008, excise tax maintained the same share to total revenues compared with the previous year. However, its growth rates moderated in 2008. With the exception of August 2008 -when excise tax reached its peak⁵⁴-, its growth rates contracted in the following months. The rationale behind mainly relates to the reflection of the reduced global oil price in the Albanian market. The projected level of excise tax has been met by 91 percent.

Profit tax revenue reduced by around 14 percent in annual terms, owing mainly to the 10 percent cut in the profit tax. The annual projection for the profit tax revenue has been met by 98 percent.

Personal income tax manifested the highest growth rates in annual terms. The positive effect of the change in the income tax, the endeavours to formalize the economy⁵⁵ and the setting of the monthly reference wage for private sector employees provided their impact in 2008. In addition to the high annual increase (64 percent), personal income tax revenues exceeded the annual projection by 5 percent.

Customs duties continue to fall owing to the various agreements aiming at the free movement of goods.

Chart 29 Budget revenues by main items as a share of GDP, 2000-2008



Source: Ministry of Finance, INSTAT, IMF Country Report 09/73, February 2009

In contrast to the previous two years' tendency, revenues from local government posted positive growth rates owing mainly to the restructuring of taxes, which are now under the management of the local government. Despite the positive growth, they met the annual projection by 86 percent.

Contributions for social and health insurance reached their record of the last four years. The broadening of the tax base for social insurance contributions - a key element in the reduction of fiscal vulnerabilities, triggered mainly by the measures taken aiming at formalizing the economy - represents a key factor in this development.

Non-tax revenues moderated their growth rate and recorded a slightly higher increase relative to the previous year. However, the difference with the projection is fairly small⁵⁶.

- BUDGET EXPENDITURE**

Expenditure for the year 2008 amounted to ALL 350.3 billion, out of which 26 percent is capital expenditure – the highest ratio in the last decade. The high annual growth rate (22.6 percent) and the high actualization of the projection are positive developments related to the performance of budget expenditure. However, the 40 percent concentration of total annual expenditure in the last quarter of the year led to volatile yields in the Government securities' market.

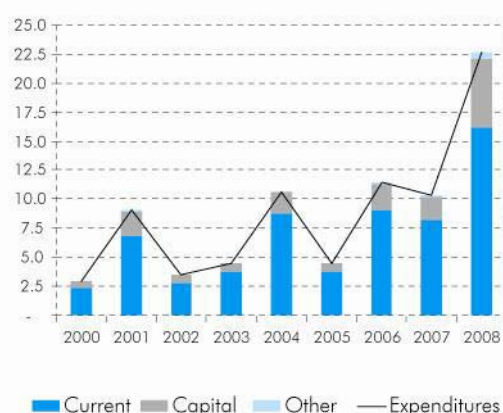
Personnel costs account for 19 percent of total expenditure. Their annual increase is 13 percent, meeting 99 percent of the projection.

Expenditure on interests (of domestic and foreign debt) as a share to total posted similar levels as in the preceding years (9 percent). Unlike the previous years, the foreign debt payment increased substantially.

Subsidies maintained their downward tendency as in the previous years, while operation expenditure preserved their growth rates as in the preceding years.

Social insurance outlays manifested an upward tendency in 2008, albeit more moderate in annual terms.

Chart 30 Annual nominal change of expenditure by main items, 2000–2008



Source: Ministry of Finance, Bank of Albania estimations

Table 17 Budget expenditure by main items

In billions of leks	Average 2005-2007	2007	2008				2008 Total
			Q1	Q2	Q3	Q4	
Expenditure	258.94	285.67	53.10	84.22	80.05	132.89	350.27
Personnel Cost	56.49	59.09	14.17	15.82	16.35	20.27	66.62
Interest	25.54	25.59	6.93	8.10	7.97	8.31	31.31
Operations	24.19	25.26	3.70	6.75	6.17	12.33	28.96
Subsidies	3.67	3.54	0.21	0.68	0.62	1.05	2.55
Capital Transfer to KESH	2.67	8.00	-	-	-	2.52	2.52
Social Insurance Outlays	61.93	69.89	16.64	18.38	20.40	20.78	76.21
Local Budget	21.35	21.34	3.78	6.69	6.73	9.93	27.12
Aids and compensations	12.92	14.77	2.61	3.34	3.50	8.28	17.73
Investment	48.84	57.04	5.07	22.95	17.49	46.86	92.37
Additional Capital Spending ⁵⁷	1.00	1.16	-	1.52	0.81	2.56	4.89

Source: Ministry of Finance

In contrast to the previous year, local budget expenditure posted positive growth rates contributing to the increase in total expenditure by about 2 percentage points.

The improved capital spending management through the reallocation of funds to large-size projects was one of the fiscal policy priorities in 2008⁵⁸.

Chart 31 Budget expenditure by main items as a share of GDP, 2000-2008

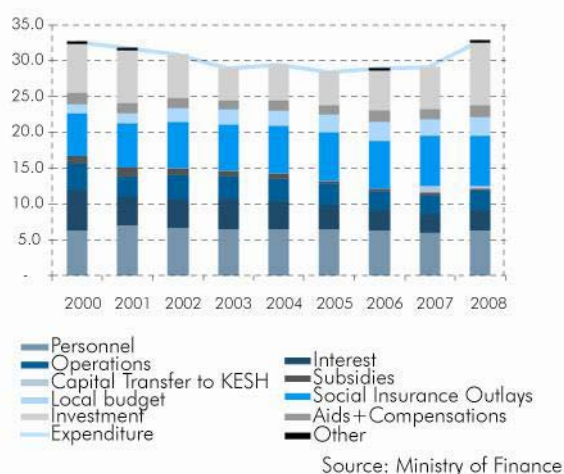


Chart 32 Annual change in the budget deficit, and foreign and domestic financing, 2000-2008⁵⁹

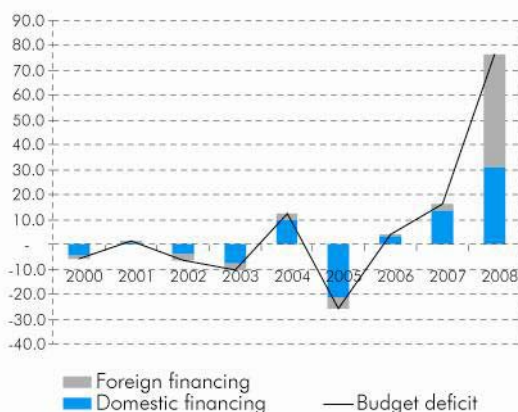
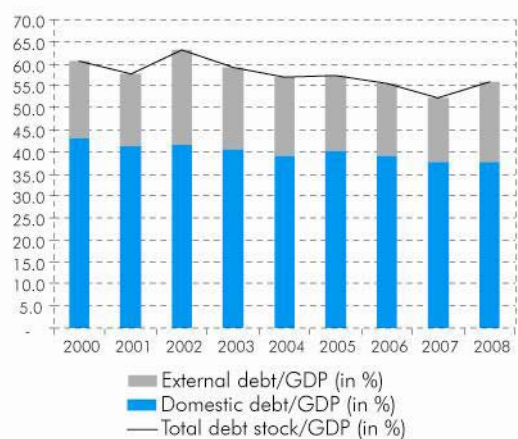


Chart 33 Public debt stock as a share of GDP, 2000-2008



The fiscal year attested to relatively higher capital spending compared with the previous years. In nominal terms, capital spending amounted to ALL 92.4 billion, a considerable fraction of which is represented by the spending on the construction of Rrëshen-Kalimash road. 54 percent of investment expenditure was covered by domestic financial resources and the rest by foreign ones. Capital spending accounts for 8.7 percent of GDP from 5.8 percent the previous year.

• BUDGET DEFICIT AND ITS FINANCING

The year 2008 posted a ALL 60.2 billion budget deficit, up by 76 percent relative to the previous year. Around 59 percent of the budget deficit was financed through foreign borrowing. As a share of GDP, it reached 5.66 percent, up by 2.2 percentage points from the previous year.

• PUBLIC DEBT

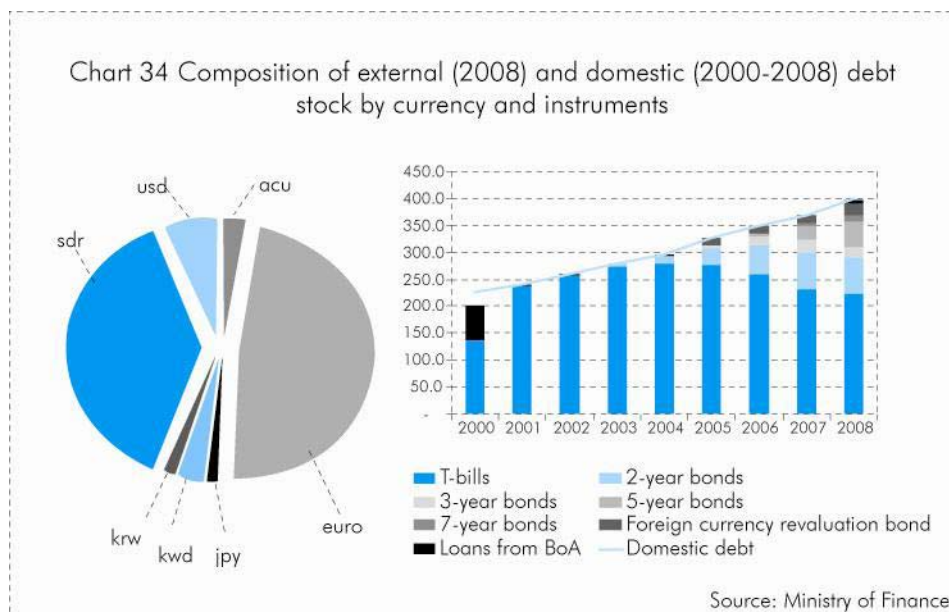
Albania's 2008 public debt accounts for 55.9 percent of GDP from 52.8 percent the previous year. The higher public debt owes to the increase in foreign borrowing for the financing of capital expenditure.

Domestic borrowing through the issue of securities increased by ALL 15 billion in 2008. Government's debt stock in 3-year bonds and T-bills reduced in 2008, increasing to a certain extent the borrowing in 5 and 7-year bonds. This reflects the strategy of the Ministry of Finance to extend the domestic debt maturity and increase the long-term debt instruments, paying special attention to the market fragmentation⁶⁰.

Foreign borrowing increased by about 29 percent in 2008 compared with the previous year, with euro-denominated borrowing sharing the largest portion. The 2008 euro-denominated debt stock accounts for about 48 percent to total external debt stock, or up by 14 percentage points from the previous year.

The improvement of the public debt management is part of the National Strategy for Development and Integration objectives. In view of this, the key components include the extension of the maturity period of domestic borrowing and from a technical viewpoint, the improvement of the securities' market

infrastructure (the establishment of the Delivery-versus-Payment system for the Government securities' trading).



With respect to the first objective, the maturity of domestic borrowing increased to 401 days from 346 days in the previous year. Put differently, long-term domestic debt shares 39 percent of total domestic debt, up by 4 percentage points in annual terms. With regard to the second objective, a number of important steps were made in 2008 for establishing the legal basis for the implementation of the Delivery-versus-Payment system, which will replace the current Book Entry system.

ENDNOTES

- ¹ The Bank of Albania defines prices stability as an annual inflation rate of 3 percent, with a tolerance band of ± 1 percentage point.
- ² Food and oil prices rose by an average of 53.9 and 41.9 percent in the first half of 2008.
- ³ In March 2008, the energy price rose by 23.7 percent in annual terms.
- ⁴ In the last quarter, this item's prices fell by 19.2 percent.
- ⁵ Mainly the higher prices in grains and processed foods.
- ⁶ The inflation measures by sectors have been revised based on the imported share of CPI basket goods.
- ⁷ March 2008 – the rise in energy price; June 2008 – the rise in urban transportation prices.
- ⁸ Measured as the weighted average of processing industry index and the unit value index for consumer goods' imports.
- ⁹ The annual increase in producer prices for these two industries in January to September 2008 was 13.8 and 14.2 percent, respectively.
- ¹⁰ The correlation coefficient attests to a stronger statistical correlation between "processed foods" for Albania and these two countries than between total consumer price index. The correlation coefficient for the period 2002M1-2008M12 is 0.9 in the first case and 0.5 in the second.
- ¹¹ Italy and Greece.
- ¹² The correlation coefficient for the period 2004-2008 is 0.8.
- ¹³ In the first three quarters of 2008, the Albanian Lek stood 12 percentage points higher than the US dollar.
- ¹⁴ The Bank of Albania's foreign reserves increased by EUR 192 million or 0.9 percentage points as a share of GDP.
- ¹⁵ The data on the GDP and its real growth for the 2001-2006 period have been provided by the INSTAT. The rest of the data are estimations of the Ministry of Finance, IMF and Bank of Albania.
- ¹⁶ The table has been constructed based on the revised nominal GDP.
- ¹⁷ Nominal GDP, converted with the average exchange rate for the period.
- ¹⁸ The data on the number of employed persons and the unemployment rate for the year 2008 refer to the third quarter, INSTAT.
- ¹⁹ The data on fiscal indicators are preliminary.
- ²⁰ Government debt including the government guaranteed debt. For the conversion of the external debt stock into the Albanian Lek, the last exchange rate of the year has been used.
- ²¹ The ETI aggregates specific indicators of the main sectors of economic activity (industry, construction and services) and consumers. The indicators' series, based on the information obtained from the confidence surveys formulated by the BoA and which are used for the construction of the ETI, are seasonally adjusted.
- ²² In more concrete terms, the Economic Tendency Indicator posted a decline of about 5 percentage points in the first quarter of 2008, to later increase by 2 and 8 percentage points in the second and third quarter of 2008. In the last quarter of 2008, it fell by 10 percentage points.
- ²³ Qualitative questions call from the respondent for a response in the form of an opinion, perception or judgement on past or expected developments in different aspects, in contrast to quantitative questions which require a number from the respondent.
- ²⁴ Empirical studies suggest that the business confidence indicator tends to perform better than the consumer confidence indicator.
- ²⁵ 2008* - It refers to the average of annual changes for the first three quarters of 2008.
- ²⁶ House Price Index and Rent Index are measured by the Bank of Albania. The measurement involves only the city of Tirana.
- ²⁷ This value is obtained by deflating the House Price Index with the Consumer Price Index.
- ²⁸ During the first nine-month period of 2008, the number of construction permits increased by 31 compared with the same period the previous year (only for the city of Tirana).
- ²⁹ The data refer to the period from January to September 2008.
- ³⁰ Among the foreign travellers, 93.7 percent were travellers with nights of stay and 6.3 percent of the total number of travellers were same day travellers.
- ³¹ In October and November 2008, the number of foreign travellers increased.

³² Budget and non-budget (INSTAT, *Conjuncture, Main Economic Indicators, July-September 2008*).

³³ In annual terms.

³⁴ Average wage is measured as the ratio of wages fund to the number of employed persons – INSTAT methodology.

³⁵ The employment rate is the ratio of employed persons to the total labour force.

³⁶ The ratio of employed persons to the individuals aged 15 to 64 years (in percent).

³⁷ The ratio of the number of employed males to the individuals aged 15 to 64 years (in percent).

³⁸ The ratio of the number of employed females to the individuals aged 15 to 64 years (in percent).

³⁹ Manufacturing.

⁴⁰ Trade.

⁴¹ The ratio of the number of unemployed males to the labour force.

⁴² The ratio of the number of unemployed females to the labour force.

⁴³ According to the data of the Ministry of Labour, Social Affairs and Equal Opportunities, long-term unemployment in 2008 reached 66 percent.

⁴⁴ In annual terms by 16 and 7 percent, respectively.

⁴⁵ The annual growth rate of exports and imports in 2007 was 24.7 and 26.2 percent, respectively.

⁴⁶ About 20 percent higher in annual terms.

⁴⁷ In 2007, Albania paid off EUR 24 million on its external debt interests.

⁴⁸ The decrease was mainly recorded in investments in the form of banking system's deposits held with non-resident financial institutions.

⁴⁹ The fiscal data for the year 2008 are preliminary.

⁵⁰ The budget projection of the Ministry of Finance was subject to revision twice in 2008.

⁵¹ The budget projection approved upon the normative act of the Council of Ministers in December 2008 was cut compared with the budget projection approved by the Parliament in July 2008 (by ALL 5.6 and 5.5 billion, respectively, for total revenue and expenditure).

⁵² The National Strategy for Development and Integration and the Medium-Term Budget Programme constitute the framework of the Integrated Planning System (IPS), a set of operating principles to ensure that government policy planning and implementation take place in a coherent, efficient and integrated manner. The IPS assists the government in prioritizing the expenditure based on the national strategy.

⁵³ The structural benchmarks involve certain areas such as the reduction of fiscal vulnerabilities, the improved management of budget expenditure and the strengthening of the financial system through the improvement of the Government securities' market infrastructure.

⁵⁴ The rationale behind is the still high fuel prices and the increase of excise goods' imports (alcoholic/non-alcoholic beverages and tobacco), in particular in August 2008.

⁵⁵ For instance, the channelling of the private sector's employed persons' wages through the banking system.

⁵⁶ The projection was not met by ALL 1.8 billion.

⁵⁷ This item includes capital transfers for the compensation of expropriated subjects and expenditure for the reconstruction of Gërdec.

⁵⁸ The fiscal authority has required from the respective ministries to formulate proposals related to more qualitative and larger-size projects and avoid small-size projects.

⁵⁹ The chart shows the contribution of foreign and domestic financing depending on the change of budget deficit.

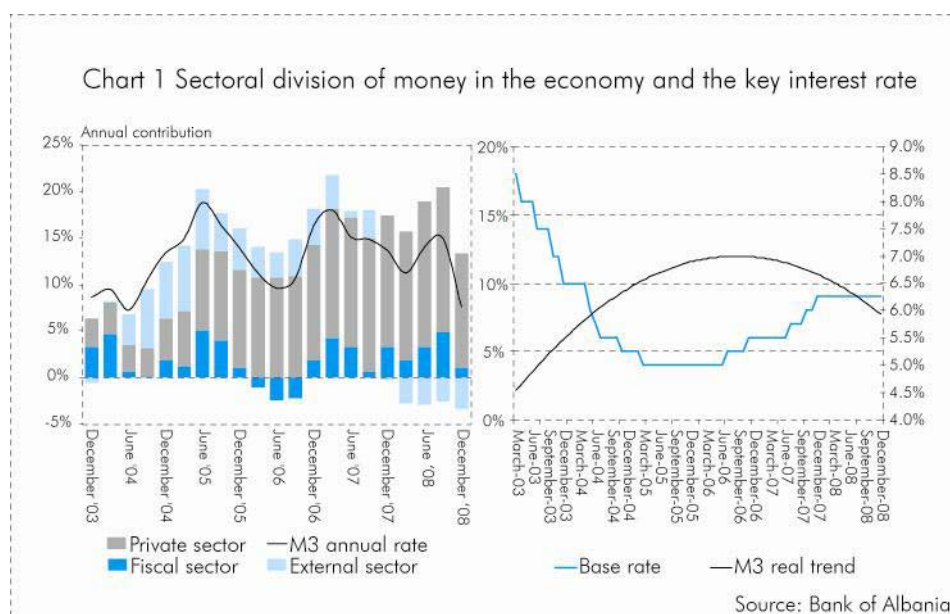
⁶⁰ In order for the instruments used in the securities market not to trigger the market fragmentation, the 3-year bonds have been matured.

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CHAPTER III MONETARY AND FINANCIAL DEVELOPMENTS

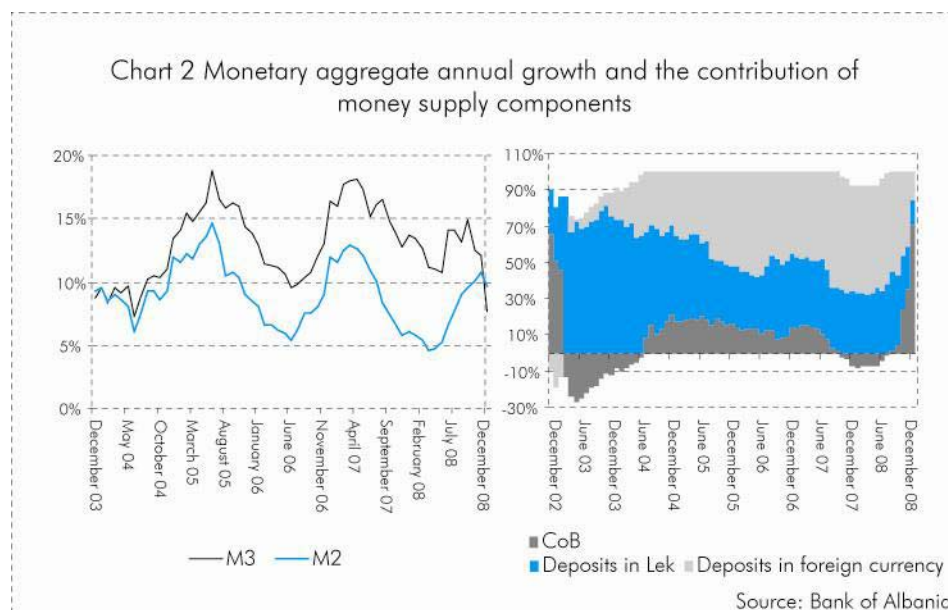
3.1 MONETARY DEVELOPMENTS

Monetary indicators performance during 2008 highlighted stabilization of money supply growth rates in line with net domestic assets performance, which reflected the economic agents' demand for money. Real M3 growth rates were falling during two last years, suggesting a better monitoring of inflationary pressures. This slowdown was conditioned even by the gradual tightening of monetary policy during this period, through key interest rate rise. During 2008 Bank of Albania's monetary policy was neutral, helping further consolidate the slowdown of monetary expansion pace. From the sectoral viewpoint, the monetary developments during 2008 reflected a higher need for financing the private sector, a lower demand of the fiscal sector and a negative contribution of foreign currency component. Private sector lending continued to generate high monetary flows, dominating the increased stock of money even during 2008. In the meantime, expansion of foreign currency credit at higher paces than deposits led to reduction of foreign currency claims of banks on non-residents and in consequence, to a negative contribution of foreign currency component to money expansion.



Monetary developments continued to be featured by the tendency to shift towards less liquid components. The average share of deposits to broad money resulted above 80 percent in 2008, compared to about 78 percent in 2007. This increase reveals the constant bolstering of confidence in the banking system and of the interest in using its instruments. The private sector's demand for money in the major part of the year was oriented towards foreign

currency, being reflected in faster M3 aggregate growth rates compared to M2 growth rate.



The average annual M3 growth rate eased to 12.3 percent, down from 15.8 percent in 2007. The M3 aggregate performance was volatile along the year, characterised by seasonal growth during summer and a relaxation of the growth rates during the last quarter. This volatility was reflected even in money performance in real terms, where the M3 aggregate pace slowed down to 8.3 percent on average in the last quarter.

During 2008 deposit developments were characterised by seasonal volatility. Annual total deposits recorded high growth paces, mainly in summer, coinciding with high foreign currency inflows. The upward trend of deposits reversed in the last quarter, recording a slowdown of the growth paces.

The deceleration of monetary aggregate growth in the last quarter was driven by uncertainties induced from the global financial markets. The average annual growth rate of deposits over this period halved relative to that of the same period of the previous year. This behaviour reflected the withdrawal of a part of deposits from the banking system. Therefore, a rapid growth of money in circulation was noted, impacting on rapid expansion of the monetary base. The induced uncertainties were also reflected in a more prudential behaviour of banks in financing the economy. The banks' difficulties in generating adequate liquidity and their more prudential policy in terms of lending were reflected in the deceleration of credit to economy growth and of fiscal sector's financing.

Box 4. Change of monetary statistics methodology

Monetary and financial statistics are an important and specific part of national macroeconomic statistics. They present, on the one hand, the financial flows among

the economy sectors, and on the other hand, the financial assets and liabilities corresponding to them. In early 2000 changes to the methodology of calculating monetary financial statistics were introduced for the first time by the IMF. These important changes were aimed at improving these statistics and adjusting them to the evolution of financial markets and instruments. New monetary statistics incorporate all the financial institutions at home, thus providing a better and rigorous coverage of the economic activity of the country.

After several years of processing and consolidating the monetary data according to new standards, the Bank of Albania has recently succeeded in passing eventually to the usage of these statistics. In the second half of 2008, the monetary indicators data in the periodical reports of the Bank of Albania were based on "Monetary Statistics" (MS) standard versus the "International Financial Statistics" (IFS) one used previously. The new monetary statistics standard includes some conceptual changes to the structure and several technical changes, which do not affect the analysis of monetary and financial indicators, but they improve the data quality in some directions.

Among the most important change is the institutional coverage, which signifies inclusion of all institutions that accept deposits and conduct business in the Republic of Albania. In this framework, the methodology of International Financial Statistics included only the Bank of Albania and second tier banks, whereas the new standard includes simultaneously the group of Savings and Loan Associations, as part of other financial institutions.

Another change has to do with the orientation of data as concerns the sectors and financial instruments classification. The new standard has in focus the financial indicators and their performance in various sectors of the economy, versus the old standard which had in focus the sectors' analysis and then the performance of indicators in each of them. In general, this standard makes a more detailed presentation of the economy sectors and financial instruments.

Besides conceptual changes, the new methodology is distinguished from the old one in classifying deposits in M3 broad money. The main change consists in excluding from the broad money the calculation of Lek restricted deposits, Lek pledged deposits and time deposits of a more-than-two-year maturity, which have restrictions as concerns their liquidity and transferability. According to the new methodology, they are transferred into the category "Deposits excluded in the broad money".

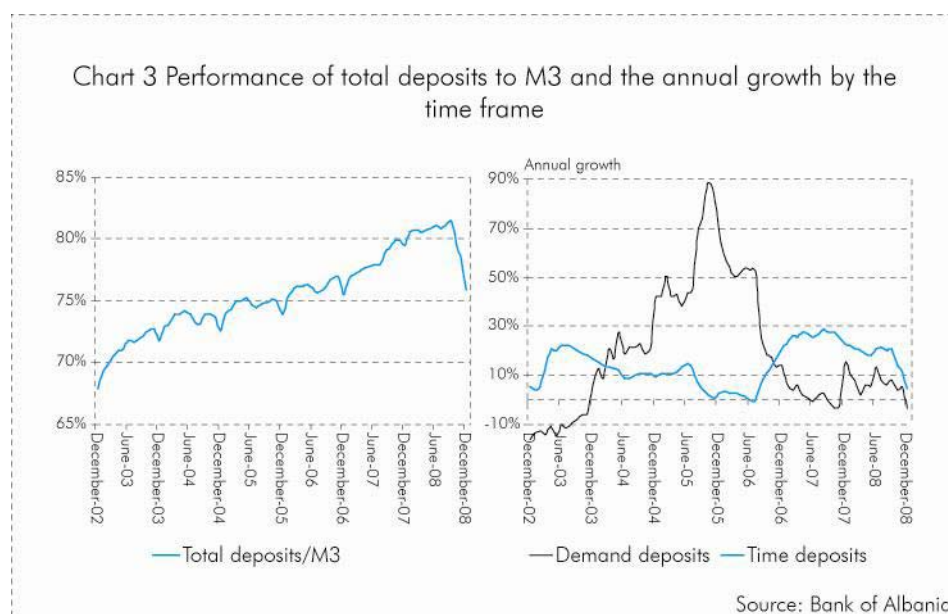
Another change to the new methodology is the inclusion of accrued interests on instruments of the Bank of Albania and second tier banks, as well as those of the savings and loan associations, newly added by means of the new standard.

Other changes relate to the terminology, which is also adjusted in line with the recommendations of international standards. For example, there is used the term "stocks and other capital instruments" instead of "capital account" or the term "non-financial public corporations" instead of "public sector".

The main weight in the change to indicators values calculated according to both methodologies consists in including restricted deposits to broad money in the old methodology and excluding them in the new standard. At the same time, of influence was also the inclusion in this standard of deposits of the savings and loan associations and of accrued interests. These changes are reflected mainly in the M1 narrow money values and in the M2 monetary aggregate in lek, while they are reflected less in the M3 broad money. However, the changes between both methodologies do not affect the entire estimation of monetary indicators for monetary policy purposes.

3.1.1 DEVELOPMENTS IN M3 TIME FRAME

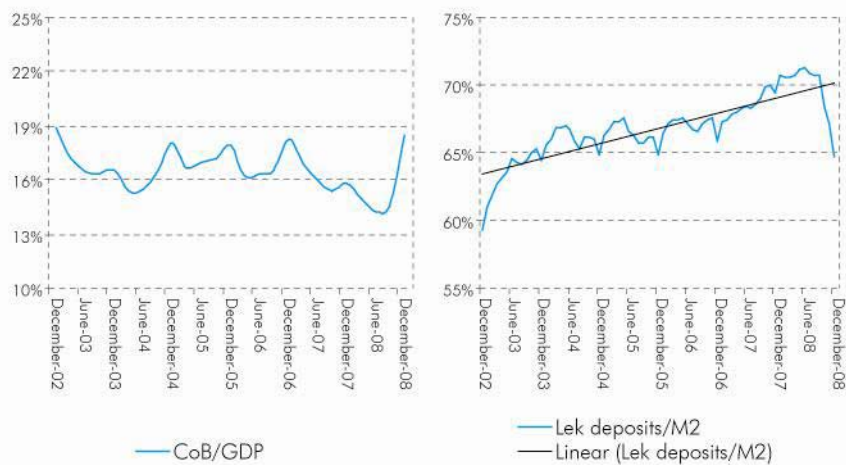
The overall time frame of money supply tended towards longer-term monetary assets. Notwithstanding the decline in end-2008, the total deposit share to M3 grew on average by 2 percentage points compared to 2007. The deposit time frame during the first half of the year underwent substantial changes. An inclination towards shorter-term components was noted by the end of the period. It was driven by uncertainties induced from the global financial turbulence. The average demand deposits share to time deposits resulted to 30.7 percent in the last quarter, about 1 percentage point higher than in the rest of the year.



CURRENCY OUTSIDE BANKS

The most liquid component of M3, currency outside banks, was volatile during 2008. In the first half of the year this indicator continued the downward trend, reaching the lowest historical levels, falling on average by - 4.4 percent on annual basis. This tendency is noticed also in the low rate of the monetary base, which in annual terms grew only by 2.2 percent in the first half of the year, compared to 11 percent it was in the same period of the previous year. By the end of the period, a rapid growth of currency outside banks was noted, impacted mainly by deposit withdrawal from the banking system. At the same time, fiscal sector pressures due to concentration of budget spending in the end of the period encouraged growth of currency outside banks. Average share of currency outside banks to M2 fell related to the previous year, though during the last quarter this ratio resulted about 3 percentage points higher than in the same period of the previous year. The growth of the system's net claims on the government by about ALL 30 billion at the end of the period encouraged the M2 expansion, mainly through its liquid component, i.e., the currency outside banks.

Chart 4 Share of currency in circulation to GDP and lek deposits to M2

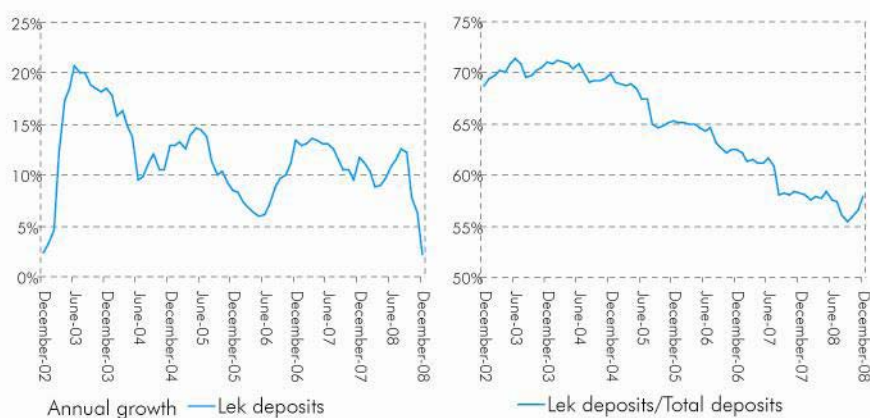


Source: Bank of Albania

LEK DEPOSITS

In medium-terms, the ALL deposit performance was steady, in accordance with the demand for liquidity and the seasonal developments in the money market. The structural composition of M2 shifted slightly towards lek deposits, regardless of the growth of the liquid component at the end of the period. The average share of lek deposits to M2 amounted to 70 percent during 2008, about one percentage point higher than in the previous year. Keeping positive real interest rates impacted on the deposit expansion. The average annual growth rate of lek deposits fluctuated around 9.4 percent, down from 12 percent in the previous year. Deceleration of lek deposit growth rate was noted in the last quarter of 2008, recording 5.5 percent. During this period the time frame of M2 experienced a slight seasonal shifting towards more liquid monetary components. The ratio of lek demand deposits to time ones rose to 28.6 percent, about three percentage points higher than in the rest of the year.

Chart 5 Annual performance of lek deposits and their share to total deposits

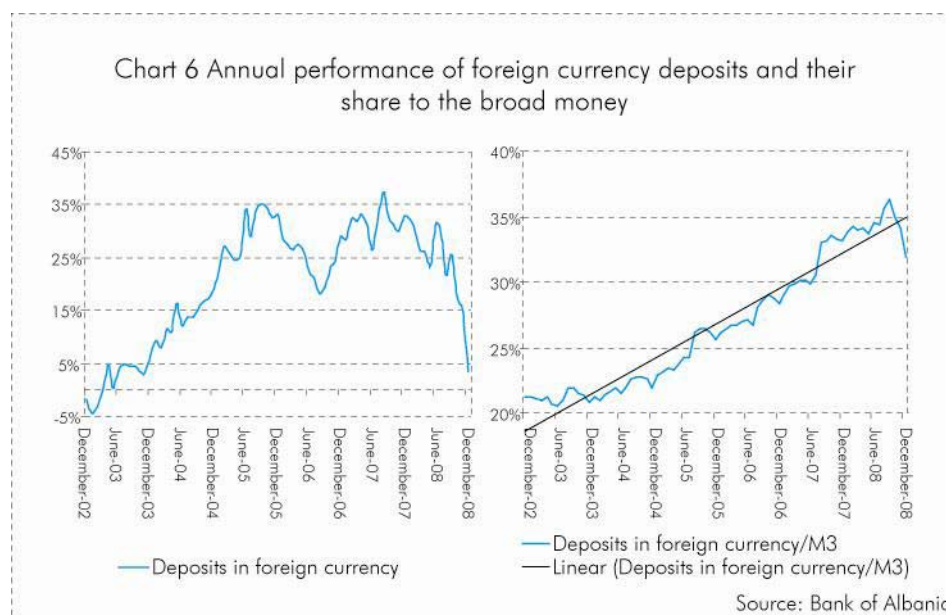


Source: Bank of Albania

3.1.2 DEVELOPMENTS IN FOREIGN CURRENCY STRUCTURE OF M3

Foreign currency component of the broad money continued the upward trend noted in the latest year. During 2008 the growth rate of foreign currency deposits was featured by seasonal volatility, whereas the annual average growth was 23.5 percent. The growth was concentrated mainly in summer, a period that coincides with high inflows of foreign currency remittances. This tendency reversed in the last quarter, where the average growth rate eased to 12 percent. Notwithstanding the slowdown at the end of the period, the average share of foreign currency-deposits to total deposits fluctuated to about 43 percent during 2008, compared to about 40 percent in the previous year.

In the long run, the foreign currency structure of the broad money was also influenced by the increasing demand for foreign currency credit, which is reflected on the supply side in the form of foreign currency-deposits. The time frame of foreign currency- deposits shifted towards longer-term monetary assets. This tendency is evidenced in the increased share of foreign currency time deposits to total foreign currency deposits, by 74 percent, about 3 percentage points higher than in 2007.



Box 5: International reserve in Albania, a comparative analysis

The monetary authority is entitled to hold international reserves of a country, which include the reserves in gold, cash-register of coins and banknotes in foreign currency, deposits held at foreign banks, various types of securities and foreign currency position at the IMF¹. Reserves' holding mainly aims at withstanding any sudden events caused by liquidity constraints in the international markets. The other face of the medal is the opportunity cost of holding reserves instead of using them as a different form of investment. The level and adequacy of reserves have continuously

been a matter of concern and debate among analysts and researchers. Quite often, various countries have been blamed for holding reserves at high levels. In a globalizing world, the high level of reserves is often motivated as an insurance against high capital mobility. Whereas, those that object this thesis think that high-level reserves are not necessary, since these funds may be used better for the development of the economy.

The strategy of the Bank of Albania in managing international reserves has foreseen a continuous growth of reserves in accordance with the constant growth of external trade activity and financial system expansion. The operational framework of reserve management pursued by the Bank of Albania has been subject to certain agreements of the Albanian Government with the IMF, such as the PRGF/EFF in the recent years. In the light of these agreements, the monetary authority has been holding a minimum level of international reserves, equal to at least three months of imports. As the agreement with the IMF came to an end in January 2009, international reserves will continuously be subject to close monitoring by the Bank of Albania.

The estimation of the optimal level of international reserves depends on a range of factors, which vary according to the economic growth and the country's progress level. Albania is a small, open and developing economy, characterized by a high and growing current account deficit, recording a fast growth of short-term foreign debt in the recent years and highly euroised broad money. In this framework, it is necessary to monitor the reserve in terms of indicators addressing to afore-mentioned characteristics of the Albanian economy. An import-based benchmark of reserves is a criterion usually recommended in cases when countries are concerned about their current account deficit, which might become a source of instability for the country. Monitoring of the level of reserves against short-term foreign debt is recommended to address risks arising from an "external drain", that is a contraction of external financial resources and to confirm the economy's payback capacity even in situations of financial crisis. Under the conditions of unilateral euroisation, the holding of reserve in terms of the broad money addresses the cases of confidence crisis, followed by sudden withdrawal of deposits.

Holding reserves in terms of the aforementioned indicators promotes better understanding of potential risk factors that might impede macroeconomic stability of the Albanian economy. Such indicators that characterize a small and open economy in terms of the balance of payments, with a highly euroised financial system as in Albania's case, render it suitable to draw on one or several conventional benchmarks for foreign currency reserves.

The recent global financial crisis has once more drawn attention to the debate on the adequacy of foreign currency reserves. Several countries have been more exposed to risks, such as further deepening of trade deficit, contraction of external financial resources or confidence crisis of the banking system, followed by sudden withdrawal of deposits. In the light of these developments, cost related issues of holding reserves are less concerning towards the need to maintain reserves at high levels in order to withstand situations of emergency.

Reserve adequacy indicators of Central East European (CEE) countries confirm an overall reduction in the reserve level since 2002 (table 1). Nonetheless, indicators of countries such as Serbia, Bulgaria, Croatia and Rumania confirm to be above the average level of the CEE countries group. Overall, Serbia has the highest level of reserves as a share of most of the indicators, while Slovenia stands on the opposite side, with the lowest level. Most of the countries, except Slovenia and Lithuania, have met the traditional minimum criterion of reserves, as they cover more than three months of imports (25 percent of the annual imports worth). In general, CEE

countries seem to have spent part of their foreign currency reserves in 2008, except Hungary and Czech Republic. Hungary's reserves increased considerably by almost 10 billion US dollars (as a result of an IMF loan disbursement), while Czech Republic reserves increased by 2 billion USD.

As of 2008, import coverage of reserves for Albania is above the average of the region countries. At the end of the year, foreign currency reserve level can cover the value of around four months of imports of goods and services. Reserve adequacy criterion as a share of GDP has fallen down to 15.1 percent in 2008, from 16.9 percent in 2002, almost 2.4 percentage points below the average rate of CEE countries. Albanian foreign currency reserves as a share of broad money stand below the average of the region countries for 2008. As such, maintaining an adequate level of reserves will continue to be in the focus of monetary policies of the Bank of Albania, even in the absence of formal agreements with the IMF.

Table 1 Foreign reserves and adequacy indicators (CEE countries)

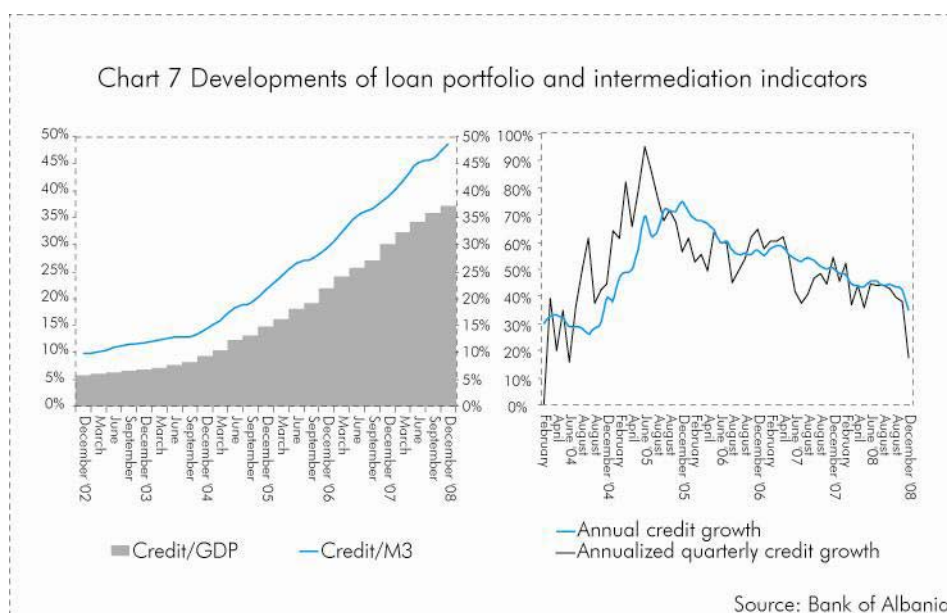
	Foreign reserve									Ratio of foreign reserves to short-term debt ¹	
	Outstanding year-end position, in USD billion			As a percentage of:							
				GDP		Imports		Broad money			
	2007	2008	Change in 2008 ²	2002	2008	2002	2008	2002	2008	2002	2008
Albania	1.7	1.9	0.2	16.3	15.4	53.8	37.2	27.8	20.1	27.9	2.0
Macedonia	2.1	1.8	-0.3	18.9	19.2	35.9	26.3	61.3	45.5	9.8	3.0
Serbia	13.9	13.6	0.4	14.2	26.0	38.6	57.4	66.7	92.3	2.1	5.0
Bosnia and Herzegovina	4.5	3.2	-1.3	19.8	16.5	34.0	25.7	47.1	34.2	3.7	1.8
Bulgaria	16.4	17.1	0.4	27.9	33.0	54.6	44.2	58.3	56.9	4.8	1.2
Croatia	13.7	12.5	-1.0	25.6	19.5	54.9	39.7	36.1	31.1	1.5	0.6
Rumania	37.2	34.9	-2.7	13.4	16.3	34.3	40.6	58.1	51.3	2.8	0.9
Turkey	73.2	70.5	-1.8	11.6	8.8	52.1	32.5	30.5	20.6	1.4	1.0
Check Republic	34.9	37.0	2.1	31.5	17.0	55.4	25.4	41.5	25.6	4.4	1.8
Hungary	23.8	33.5	9.8	14.6	20.4	25.7	30.3	27.6	47.2	1.1	1.1
Poland	65.7	62.2	-3.6	15.0	11.0	54.0	29.9	35.2	28.8	2.2	1.8
Slovakia	18.0	17.9	0.8	36.0	17.8	50.4	23.5	49.7	34.7	3.4	1.5
Slovenia	1.1	0.9	-0.2	29.5	1.7	65.0	2.7	45.1	3.6	5.3	0.1
Estonia	3.3	4.1	0.6	13.7	16.3	20.8	24.4	32.9	39.1	0.4	0.6
Latvia	5.6	4.2	-1.2	13.3	12.5	30.6	26.4	38.4	37.3	1.6	0.4
Lithuania	7.6	6.2	-1.8	16.2	12.7	30.5	19.6	51.0	38.5	1.6	0.9
Average ³	21.5	21.4	0.0	19.2	17.5	41.5	32.4	43.9	40.5	3.1	1.6

¹ Short-term external debt as defined according to the standards of the Bank for International Settlement, with a maturity of up to one year. ² Change since end 2007. ³ Simple average of the above, excluding Albania in 2002.

Source: BIS, IMF, national data and the Bank of Albania

3.1.3 CREDIT TO THE PRIVATE SECTOR

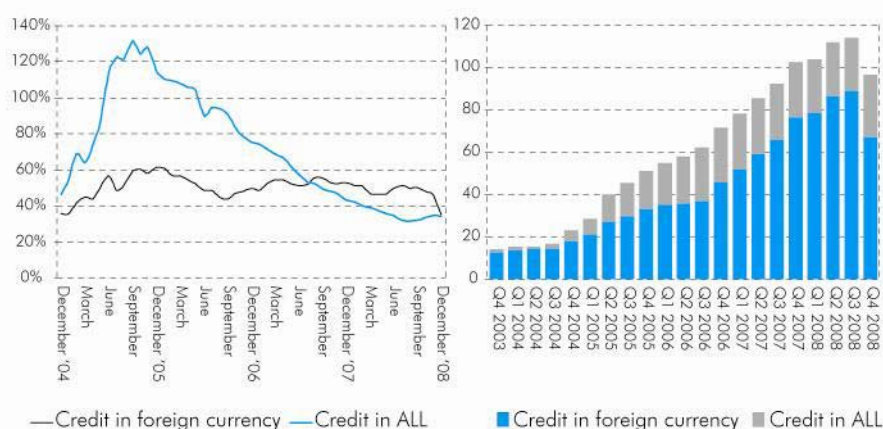
During three latest years lending to the economy increased steadily, indicating the largest sustaining the banking system has given to expansion of production and growth of the economic activity at home. During this period, the ratio of credit to gross domestic product increased on average by 7 percentage points per year, peaking by 8.2 percentage points in 2007. In 2008 this ratio increased by 7.3 percentage points, reaching 37 percent. Lending to the economy accounts for 50 percent of the broad money and 47 percent of assets of the banking system.



Lending to the economy during 2008 was expanded at slower annual rates than in the previous year, averaging 44 percent². However, in absolute value, the annual rate of credit expansion was upward for the major part of the year, reflecting the largest involvement of banks in lending and improvement of intermediation indicators. In December 2008 lending to the economy noted the lowest monthly growth in recent years, reflecting the banks' liquidity constraints, tightening of lending terms and a lower demand for credit. For the first time over 5 last years, in December, the annual credit expansion decreased substantially in absolute terms, recording an annual growth rate of 35 percent. In general, the whole '2008 was characterised by tightening of lending standards, in response to Bank of Albania's regulatory measures. In the second half of the year³, a greater-than-expected tightening of the lending standards was observed. Another factor that influenced the dampened demand for credit is also the uncertainty for the future of the economic activity at home and for performance of economic agents' income.

Foreign currency credit structure developments during 2008 revealed a slight shifting of the loan portfolio towards foreign currency one. In most of the year, credit in foreign currency grew at high and steady annual rates, on average by 50 percent. Foreign currency loan portfolio, likewise a year ago, was dominated by euro-denominated loans, accounting for 90 percent of the outstanding foreign currency credit. The preference for foreign currency loans is attributed to their lower interest rates. This factor is qualified as the most important one in the survey on the lending activity with banks. However, the Bank of Albania has concluded that commercial banks' clients do not pay due attention to the exchange rate risk, when they choose a foreign currency-denominated loan. Also, according to the survey results, generating income in foreign currency and pricing some products in euro are other important factors contributing to the preference for foreign currency loans. Even the last factor does not indicate a rational behaviour of households, since they take over a long-term exposure⁴ to exchange rate moves, versus the cost of converting credit from ALL into Euro when making the payment.

Chart 8 Annual credit growth by currencies (in percentage and in ALL billion)

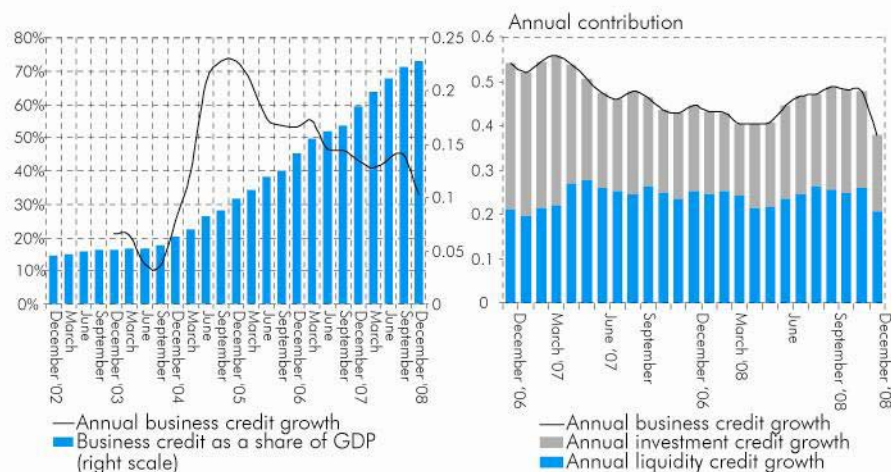


Source: Bank of Albania

Credit in ALL for the fourth quarter of 2008 reflected a moderate annual growth rate of 35 percent, equal to that of credit in foreign currency. The significant contraction of annual growth of foreign currency loan portfolio testified the banks' foreign currency liquidity constraints, impacted not only by its shortage in the interbank market, but also by higher withdrawals in foreign currency deposits. This situation made banks perform a better credit risk assessment and be more prudential in extending foreign currency loans.

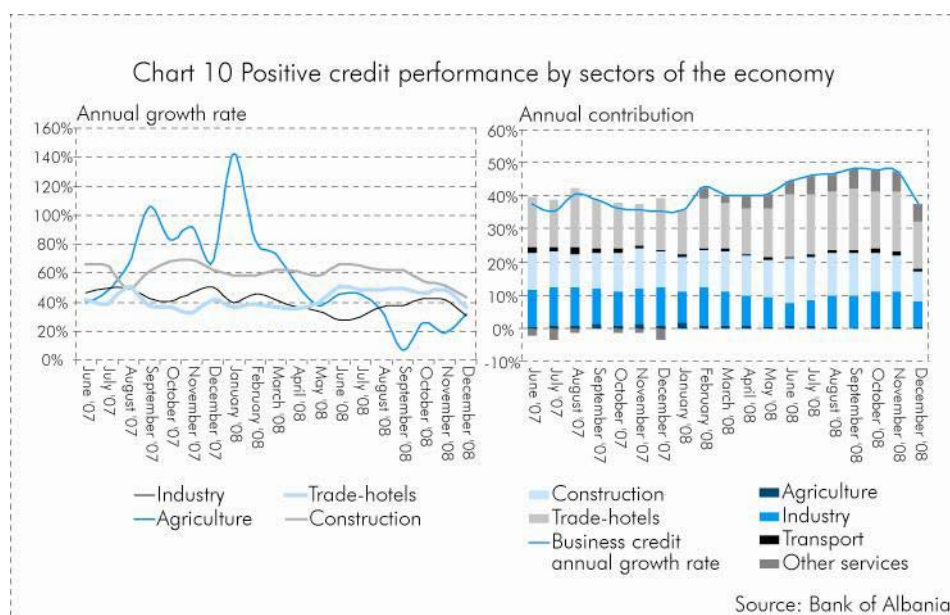
Businesses were the most preferred bank clients over 2008. Business credit portfolio indicated a high and steady growth during most of the year, on average 44 percent. Banks extended more loans to businesses, in order to meet their needs for liquidity and to finance investments in real estates. Credit for investment in machinery continued decelerating, in line with the downward trend noted in 2007.

Chart 9 Performance of business credit portfolio

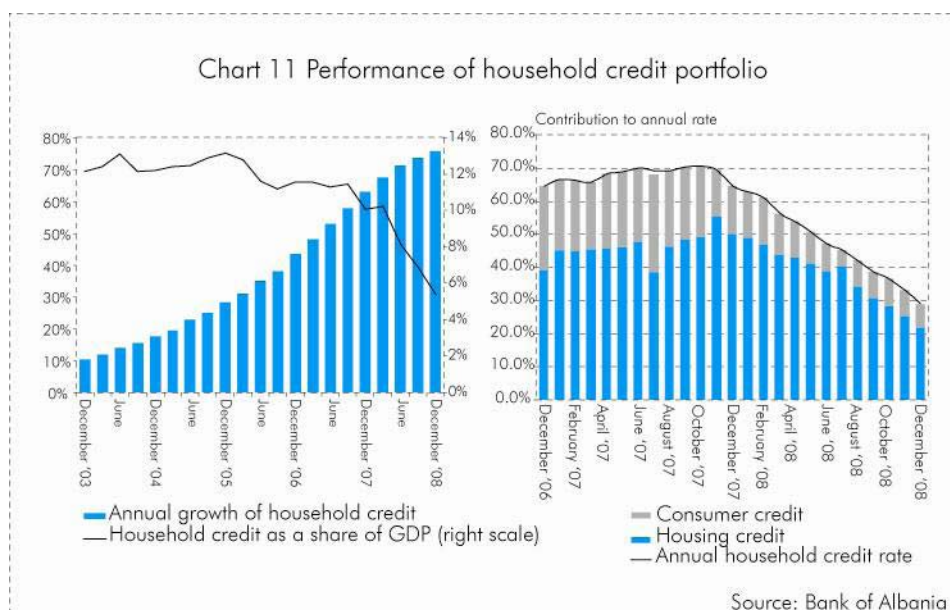


Source: Bank of Albania

During 2008 commercial banks continued to sustain with loans the main sectors of the economy, such as trade, construction and industry. The ongoing credit growth for construction - averaging 59 percent in 2008, against 63 percent in 2007 – has raised the credit weight for construction to total business credit by 2 percentage points, to on average 22 percent for 2008. Trade credit grew almost at similar paces to those of the previous year, keeping unchanged the business credit portfolio share, to 38 percent. Notwithstanding the positive developments for most of the year, both sectors reflected an obvious slowdown during last two months of the year. Industrial loan grew at lower paces than those of the previous year, on average 37 percent⁵. Therefore, the share of credit to this sector decreased by 1 percentage point at year-end, accounting for 25 percent of business credit portfolio.

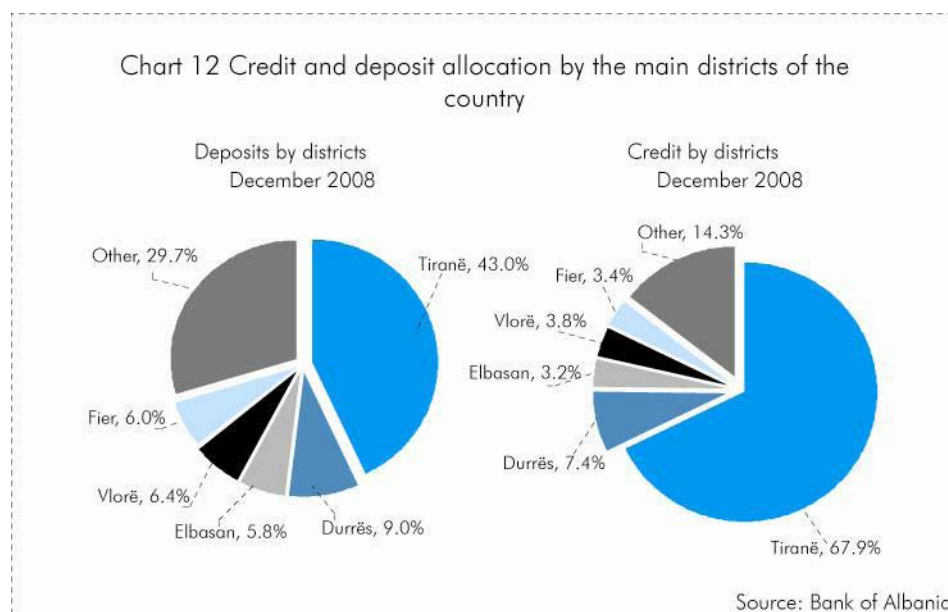


The annual growth rate of household credit slowed evenly throughout the year, dropping to 30 percent compared to 62 percent in end-2007. This



made the household credit portfolio share fall to 35.6 percent at year-end, down from 36.7 percent in October 2007. Household credit slowdown was noted for both, housing and consumer loans. Real estate loan dominated the household credit portfolio by 66 percent. It rendered the main contribution to expansion of household credit outstanding and to growth of foreign currency credit for 2008. Uncertainties induced on the performance of households' income from domestic labour market or from alternative foreign sources, made banks become more conservative and prudential in retail banking. This fact has been confirmed even by bank credit officers, stating tighter credit standards for this group as compared to businesses.

Geographical allocation of resources and fund usage indicates that the depositing activity is less concentrated than the lending one. Deposits at the capital account for 43 percent of total deposits of the system. Fund investment in assets indicated an obvious concentration of loan portfolio to the capital, by 68 percent. Geographical distribution of savings collection and loans investments indicates a more active behaviour in terms of savings collection and a more conservative one in terms of funds investment. Also, it is in line with the economic activity concentration in the main districts of the country, where most of businesses are located. However, high concentration of lending in Tirana is also related to the technical aspects of approving large-amount loans, above a certain level, only by the head-office, without reflecting the real coverage with financing of the geographical areas of the country.



Box 6. Lending activity in Albania, a comparative analysis

Many economists assess that the Central and Southeast European countries have undergone a successful economic boom and development over 5 latest years. The

living standards have improved significantly and currently these economies are integrated with the rest of Europe. The banking sector in Central and Southeast European Countries was very attractive to foreign investors (mainly European ones), due to high profits, expectations for a high economic growth and the close perspective of many region countries to be part of the European Union. Also, the financial markets of these countries, though reflecting a significant progress, have provided the necessary space for further expansion and extension of the financial intermediation.

One of the outcomes of economic integration of the Central and Southeast European countries is also the accumulation of economic imbalances, which have brought about high current account deficits and greater dependence on global market developments. While these imbalances seemed controllable prior to the financial crisis shock, now they have become problematic. Nowadays the economists are concerned about the rapid change of macroeconomic conditions in the fragile economies of these countries. In particular, they are concerned about the significant economic contraction; rapid depreciation of national currencies, high current account and fiscal deficits, as well as domination of foreign currency loans, which exert pressure and bring about concern on the country's banking activity development.

The main weakness of the Central and Southeast European countries does not stand on their exposure to toxic financial instruments, but on their high degree of integration with the global economy and in consequence, on the dependence created due to its developments. In the latest statements of the International Monetary Fund, year 2009 is foreseen as a difficult year for these countries and their economic growth is expected to decline significantly. The main shock to these countries will be given by trade, where exports are forecasted to decrease obviously, leading to a further deepening of external imbalances. Another problem will be the financing of the created deficit. The international investors, due to high uncertainties for the future, will apparently reduce investments in these countries. Also, remittances from abroad, which are envisaged to decline significantly because of the economic downturn in the developed countries, are an important financing source for these countries. Moreover, the borrowing cost has been raised, due to great uncertainties and lack of ample liquidity in the market. All these shocks will have a significantly negative impact on foreign financing for these countries.

During latest years, private sector lending of those countries increased at high paces, on average by 25 percent, or 2.5 times more than the average of EU countries. Data indicate that the fastest credit growth in the latest years is recorded by Rumania, followed by Bulgaria and Albania. In this regional panorama, Albania continues to be ranked among last countries in the share of loan portfolio to the country's GDP. What catches the eye is the fact that the ratio of banking system assets to GDP is at the highest levels in the region, being ranked very close to the levels of the new EU member states. This indicator shows that our banking system has the necessary capacity to play a high role of financial intermediation. In three last years, the banks' credit portfolio constitutes on average only 50 percent of the deposits collected by them. However, it is worth noting the fact that over the last years, the credit portfolio growth rate has been high, underlining the largest involvement of banks in meeting the economy demand for funds. The average annual growth of credit portfolio in Albania by 44 percent is currently the highest growth of this indicator for the region countries for 2008.

Table 2 Intermediation indicators performance in Central and Southeast Europe

In % for 2008	Albania	Turkey	Rumania	Bulgaria	Macedonia	Serbia	Croatia	Hungary	Poland	Czech Republic	Region average
Assets/GDP	86.9	65.5	64.9	88.1	67.8	58.6	97.4	99.8	57.2	111.8	79
Credit to private sector/GDP	36.1	31.2	39.2	74.0	43.6	38.7	71.6	64.3	49.2	49.8	51
Foreign currency credit /GDP	25.8	24.5	22.0	39.80	9.7	17.5	47.2	41.8	12.0	7.0	25
National currency credit /GDP	10.3	3.5	19.8	33.4	33.9	21.0	24.3	22.6	32.0	46.5	26
M3/ GDP	76.1	41.2	33.1	68.7	51.2	13.2	74.0	56.1	52.6	71.4	51
Total deposits/ GDP	57.8	27.0	27.0	53.1	46.3	31.9	65.3	53.2	45.0	59.8	45
Households deposits/ GDP	47.5	14.1	16.0	32.1	21.5	17.7	38.3	26.1	26.3	38.7	26
Foreign currency deposits/GDP	24.3	12.9	9.9	26.8	21.7	21.7	37.3	14.2	8.5	6.2	18
Mortgage loan /GDP	8.3	4.0	3.5	9.9		5.0	10.0	12.4	11.7	15.3	9.0

Source: Central banks' websites and BIS publications

Also, another feature of joint developments of credit portfolio of these countries was also the accelerated expansion of credit to households. Recently, this credit (especially the mortgage one), increased rapidly, driven by interest rate cut and growth of households' wealth position. Though welcomed, the rapid credit growth was viewed with concern, since it has contributed to deepening of macroeconomic and financial imbalances in these countries. In particular, the rapid credit portfolio growth has supported the domestic demand expansion, impacting on current account deterioration. Also, in many of those countries, the rapid expansion of loan portfolio is financed through foreign funds, making the banking system more sensitive to international developments. Another important concern for these countries is the high euroised loan portfolio. Recently this phenomenon has been influenced by the entry of foreign banks of regional importance, which have encouraged lending in foreign currency. This risk is assessed as higher in these countries, since most of households have received credit in foreign currency and are unhedged against exchange rate fluctuations.

Unlike region countries, credit to economy in Albania has been mostly sustained by domestic fund sources, mainly households' savings, bringing about a lower exposure to global situation. Furthermore, the expansion of this credit has mostly sustained the economic activity of businesses and less that of households, while household credit has financed mainly the primary house purchases. House price developments in Albania have been mostly influenced by the real demand of households for improving their living conditions and as such, the real estate market in the country does not present speculative developments. All these factors contribute to less exposure of our country to global developments, compared with the above-mentioned countries.

3.2 FINANCIAL MARKET DEVELOPMENTS

Financial market activity was relatively stable during 2008. The financial markets at home continue to be featured by a low degree of development and integration with the neighbouring markets or beyond. This feature was turned into the "favour" of the financial stability, helping them hedge against the

financial crisis that has affected the European countries. The psychological consequences of this wave led to deposit withdrawal in the last months of the year. This induced uncertainty in the banking system over the last quarter, making interbank market interest rates highly volatile. In order to meet their needs for liquidity, some banks decreased their participation in the primary market, leading to yield rate rise in two last months of the year. Bank of Albania's intervention through injecting liquidity to relax and ensure the market agents provided a positive impact, reducing the interest rate volatility in the interbank market by year-end.

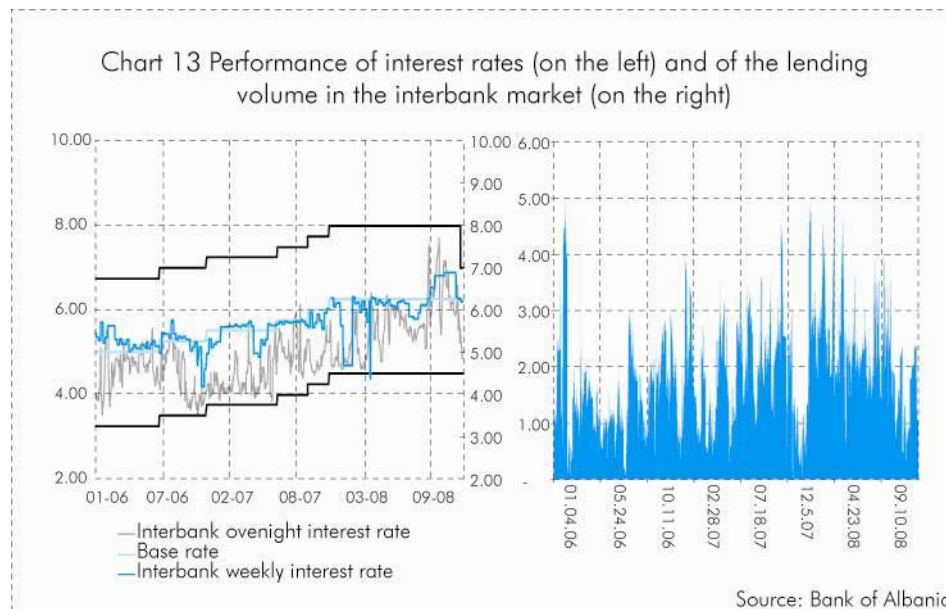
Deposit interest rates indicated upward trend for both, the national currency and the euro. In spite of decreased interest rates of the euro in the international markets, the banks have preferred to keep relatively high levels, in order to attract euro funds in the domestic market. The interest rate spread resulted positive and on average higher than in the previous year, sustaining the national currency. During the major part of the year the lek's exchange rate against foreign currencies was steady, starting to depreciate slightly by the end of the period. The lek's depreciation coincides with the trend of the performance of all currencies of East Europe and carries over the psychological factors and the changed demand/supply ratio in the market.

In contrast to deposit interest rate performance, the credit interest rates were downward. This helped narrowing the spread between both indicators and reducing the intermediation cost of the banking system. Positive is the evidence on raising attention in lending in ALL and the competition through interest rates in this market.

INTERBANK MARKET

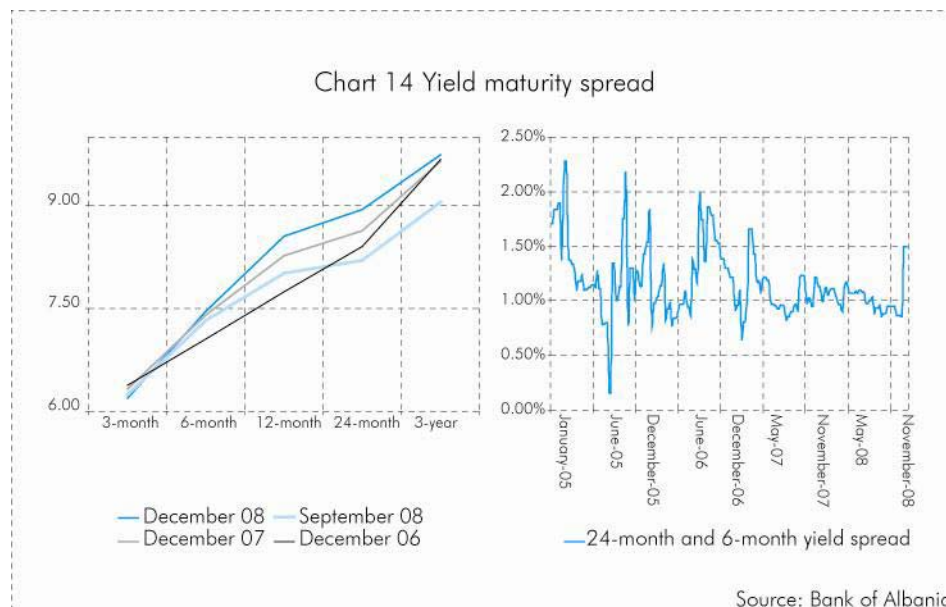
The interbank market was featured by high interest rate volatility during 2008, making them swing from the minimum theoretical levels (overnight deposit) to the maximum one (overnight loan). Until September the interest rates fluctuated below the base interest rate, being raised at the moment of calculating the required reserve. Structural liquidity shortage during this period created better conditions for monetary policy transmission; impacted on approximating interest rates in the interbank market to base rate; and promoted the activity in the interbank market. The spread between the overnight interest rate and the base one for this period is estimated at about 70 basis points, from 90 basis points in the previous year. Average daily volume of lending amounted to ALL 2.3 billion, from ALL 1.8 billion in the same period of the previous year. In spite of the trade volume growth, a relatively high concentration of funds and a limited presence in trading among banks, remain features of the interbank market. These obstacles became more pronounced during September-November - at the moments of fulfilling the required reserve (September), the interest rate rose to 7.54 percent or 129 basis points above the repurchase agreement rate⁶. Under the concern for finding liquidity in the wane of deposit withdrawals (November), the overnight interest rate amounted to 7.16 percent or 91 basis points above the repurchase agreement rate. Average lending volume is estimated at ALL 1.6 billion for this period, thus recording a decline. The Bank of Albania's

intervention⁷ to ensure real and psychological support to the market, gave effect on cutting the cost of liquidity provision to the interbank market and decreasing the volatility of this indicator. During December the overnight interest rate dropped to 5.84 percent, the average level of the year.



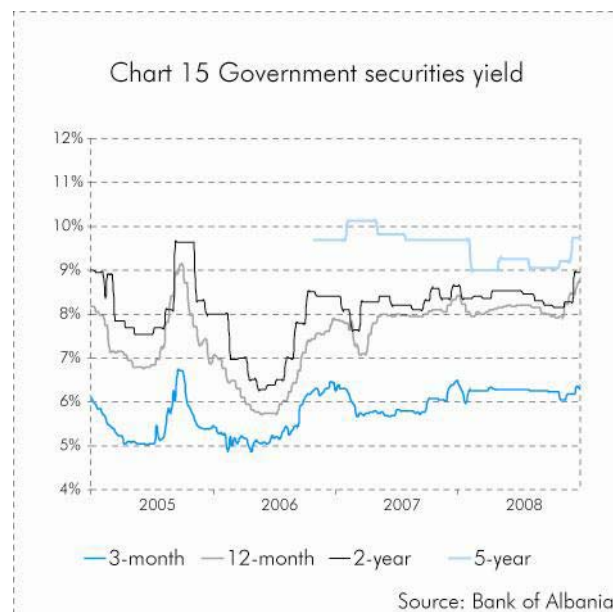
PRIMARY MARKET AND YIELD PERFORMANCE

Treasury bill yields in the primary market were relatively stable during most of 2008. Their volatility was influenced mainly by market structure factors. During first months of the year they transmitted the base rate rise effected during end-2007, being reflected in an upward trend, whereas their reduction is noted in the third quarter, after the creation of high liquidity balances in the market. The 12-month T-bill yield was estimated at 7.94 percent in October, from 8.23 percent in January. During the last two months of 2008, yields rose, transmitting the liquidity tightening position in banks as a combined effect of



deposit withdrawals and increased demand by the government. In most T-bill auctions, the required amounts and the participation were at adequate levels.

The bid/cover ratio in auctions recorded high values. The downward yield trend noted mainly in the third quarter, reversed during the last months of the year, when the tightened liquidity position and the high demand for financing led to their increase. Notwithstanding Bank of Albania's intervention to provide the system with liquidity, during this period banks' reluctance to invest in the primary security market was noted. The low participation in auctions led to yield rise. In December the 12-month yield resulted to 8.56 or 0.30 percentage points higher than in the same period of the previous year. The 3-month yield for 2008 averaged to 6.25 percent, equal to the base interest rate, whereas the 6-month yield followed the same trend as the 12-month one.



During this year banks' preference to invest in long-term instruments continued to grow and the demand for them was satisfactory. At the same time, the yield performance was volatile, depending on the changed supply/demand ratios in the market. During the first half of the year they followed a stable performance and with downward trend, concentrated mainly in the third quarter. The spread between maturities dropped, smoothing the yield curve slope. It's worth noting the narrowing of the yield spread between 5-year bonds and 2-year ones, which reveals improvement of the perceived risk premium by agents for these long-term instruments compared to the period when they were issued for the first time.

The average yield of 2-year bonds rose by 0.15 percent in 2008, compared to 2007. During the last months, banks' demand was conditioned by market liquidity constraints, being transmitted to low participation and high yields.

FOREIGN EXCHANGE MARKET AND EXCHANGE RATE PERFORMANCE

The effective nominal exchange rate has reflected a wide range of developments throughout 2008. The national currency continued to appreciate against the basket of the major currencies during January-April, peaking in April (6.2 percent in annual terms). Both following quarters reflected a slowdown in annual growth rates (1.4 percent in September), passing to depreciation in the last quarter of the year (on average -3.2 percent).

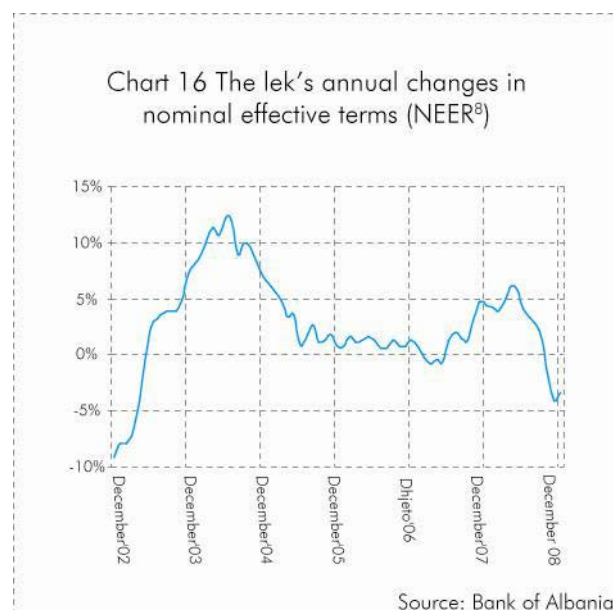
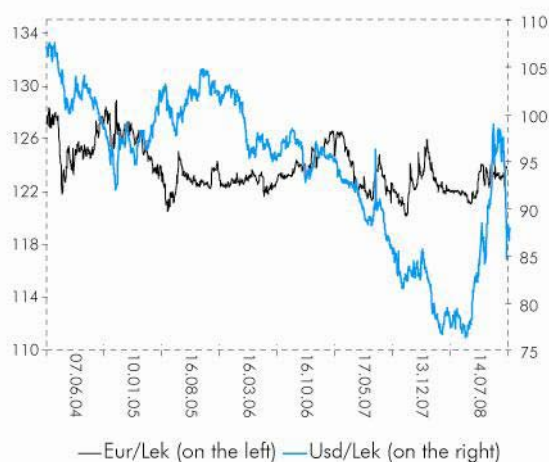
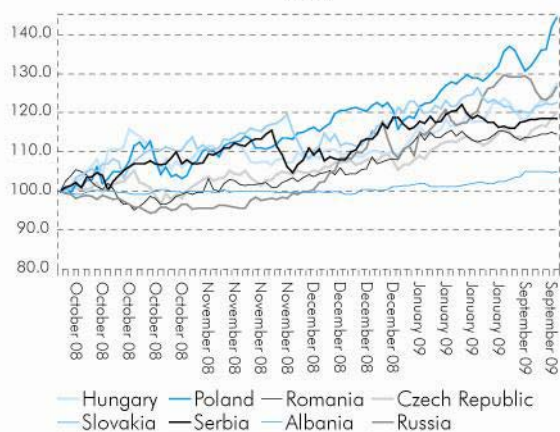


Chart 17 Daily exchange rate performance of the euro/lek and the usd/lek



Source: Bank of Albania

Chart 18 Euro's performance against East European currencies (index base October '08 = 100)



Source: Central banks of respective countries

Chart 19 Average rate of the Euro-national currencies for East Europe



Source: Central banks of respective countries

At end-2008 the lek's exchange rate against the euro and the US dollar reflected an annual decline by 0.37 and 10 percent respectively. However, in average annual terms, the lek strengthened by 0.66 percent and 7.23 percent respectively against the euro and the US dollar during 2008.

Regardless of last quarter developments, it's worth noting that the positive performance of the national currency was sustained by a number of factors, such as: satisfactory performance of macroeconomic indicators at home, positive result of the balance of payments, inflation anchoring close to Bank of Albania's target and the approximation of this indicator to that of the developed countries (Euro-zone), as well as the positive interest rate spread.

Domestic foreign exchange market activity grew constantly, not only due to trading activity enlargement, whose total growth is estimated to 31.1 percent in annual terms for 2008, but also due to increased professionalism of market participants. The latter present a more and more preceding behaviour towards the exchange rate seasonality. In concept, this does not change much from the forward⁹ transactions effected in developed financial markets, where actors try to reflect exchange rate expectations, helping in weakening the seasonal effects. In this line, there is also highlighted the fact that the isolation of the Albanian financial system from sophisticated products of international financial markets, which proved to be the creators of the global financial crisis, helped inhibiting the penetration of effects that some advanced European economies (Great Britain, Ireland, Norway)¹⁰ and those of East Europe are going through. Visualising the euro's performance against the currencies of the East Europe during the last quarter of the year, it is noted that in relative terms, the lek's performance is stable and with a significantly lower volatility.

Analysing the exchange rate dynamics in the domestic market, it comes out that the euro/lek ratio volatility was moderate as compared to the previous year and to the time frame of 5 years. On the other hand, the US dollar presented a significantly higher volatility against the lek, due to the dynamic performance of the US dollar in international markets.

DEPOSIT AND CREDIT INTEREST RATE PERFORMANCE

Generally, the deposit interest rates were raised for both the national currency and the European one during 2008. Though the base interest rate remained unchanged, the ALL deposit interest rate increased during the second half of the year, due to successive presentation of limited time promotional offers. Though summer and year-end are usually characterised by attractive offers in an effort to absorb deposits, during 2008 this behaviour became more emphatic, making interest rates reach historical peaks in years.

In 2008, in the medium-term the ALL deposit interest rate averaged 0.92 percentage point higher than in 2007. This move carries over the rise by 0.75 percentage point of the base rate during 2007. The average interest rate of lek deposits fell in the first months, from 5.43 percent in January down to 4.99 percent in March, due to termination of offers of the past year-end by commercial banks. Since April and onward this indicator increased, reaching record levels in August, by 6.72 percent, due to aggressive offers promotion. It seems that this strategy was related with individual policies of banks to increase their market share. September recorded interest rates cut by 0.61 percentage point and a tendency to revert them to previous levels. The psychological effect caused by the news, related to uncertainty induced in the financial markets over the last quarter, inhibited the corrective tendency and led to other short-term offers at end of the year, in an effort to retain the financing resources.

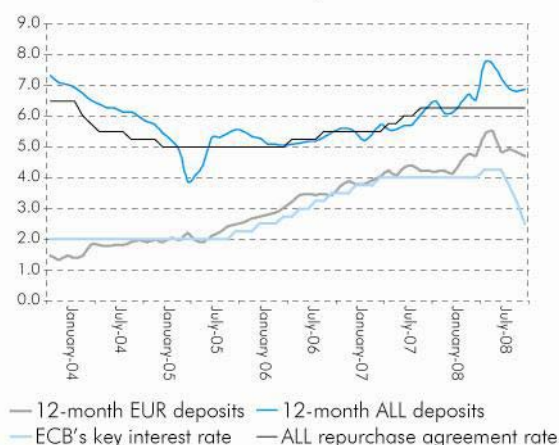
Euro time deposit interest rates in general were featured by an upward trend during three first quarters of 2008. This trend started in January and peaked in August, averaging to 4.22 percent or 1.21 percentage points higher than in the previous year-end. The upward trend over this period was affected by the change of the ECB's key interest rate by + 0.25 percentage points, as well as by certain banks' promotions to attract foreign currency remittances. It seems that in the last quarter the ECB's aggressive easing policy was orienting but not a determinant factor on euro-denominated time deposit interest rates in the country. The latter were formed by the tendency to strengthen the deposits

Chart 20 The Lek's volatility against the major currencies¹² (annual mean)



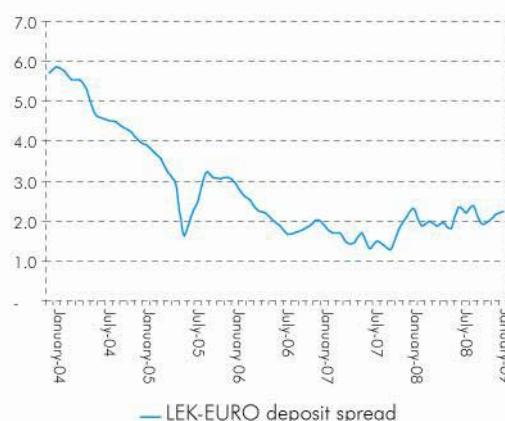
Source: Bank of Albania

Chart 21 Interest rate performance of Lek and euro deposits



Source: Bank of Albania

Chart 22 The lek- and the euro-deposit interest rate performance



Source: Bank of Albania

value, as a public investment instrument, under the conditions of increased uncertainty perception. In end-December the 12-month deposit interest rate recorded 4.70 percent or 0.03 percentage point below the average of the whole year, highlighting a high competitive tendency of the banking system for euro-denominated deposits.

High interest rates have led to a spread¹³ of 2.16 percentage points at end 2008 or 0.04 percent higher than in December 2007. On average terms, this indicator is estimated at 2.07 percent or 0.46 percentage points higher than that of 2007, influenced by positive moves of lek-denominated time deposit interest rates.

Credit demand continued to be high during 2008. This led to credit interest rate cut, mainly for those denominated in lek, in which banks reflected competitive tendencies (especially after the signal by the Bank of Albania to encourage the ALL loan portfolio growth. Seasonally, the interest rates have been influenced by the aggressive policy of certain banks that hold a significant market share.

In 2008 the weighted average interest rate on credit in ALL was 12.82 percent, from 13.57 percent in the previous year. The new credit was mostly extended for short-term financing (*overdrafts to businesses*), for financing consumption and for real estate purchases by households. The latter were promoted by interest rate cut in the last quarter. During the first quarter the interest rate for lending in ALL was downward, following the same trend as the interest rate they are indexed with - 12-month treasury bill - and in March it recorded the lowest rate in the year, 12.25 percent. In the beginning of the second semester the banking system revealed a tendency to pursue tightening lending policies. Along with application of more severe standards, a part of these policies was reflected in interest rate rise. During the last two months of the year, the lending activity revealed a shifting tendency towards the national currency. This policy brought about interest rate cut for loans in ALL, in spite of

the interest rate rise in other markets. In December, the average rate of credit in ALL dropped to 11.71 percent, hitting the lowest rate in last four years, recording the deepening of the lending activity. This development reflected the positive tendency of the banking system to finance in the national currency, contributing at the same time to intermediation cost cut in the system.

Generally, lending in euro coincided with international financial markets developments, complying with the changes in Libor and Euribor, though not at the same margin. Weighted average interest rate for euro-credits recorded 8.19 percent in 2008 compared to 8.43 percent in 2007. This indicator reached the peak by 8.70 percent in September. The rise was triggered mainly by

Chart 23 Weighted average interest rate for lek- and euro-denominated loans

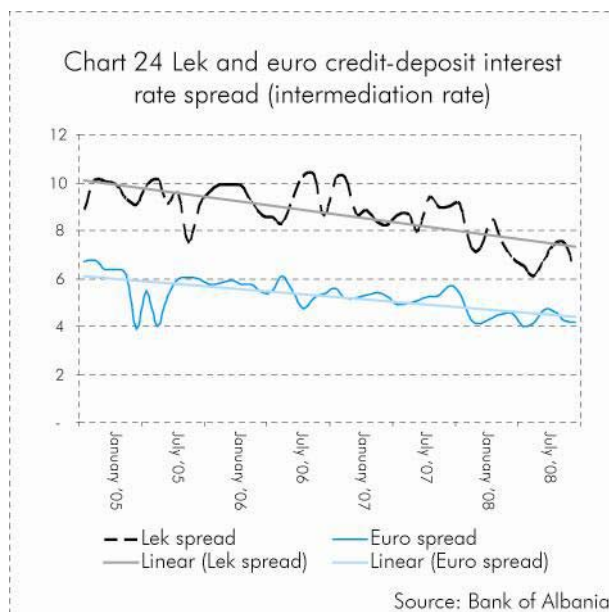


Source: Bank of Albania

the assessment for funds cost expensiveness in international markets (September coincides with the turbulence in international financial markets), the tightening policies followed by the banking system and the added risk perception. During the last months of the year, the euro-credit interest rates fell, after the reference interest -Euribor and Libor – declined in the international market. Regardless of the performance of the latter, the euro-interest rates continued to be relatively high at the end of the year, in the framework of tightening of the lending standards and application of relatively larger margins for euro-credits.

Intermediation cost (credit-deposit spread) in lek and in euro continued dropping during 2008. On average terms this indicator resulted 7.2 percentage points for the lek, down from 8.9 percentage points in the previous year. Average intermediation rate for the European currency was 4.41 percentage points, down from 5.25 percentage points in the previous year.

The lowering of lek-credit interest rates has narrowed the spread with those in euro. This indicator is estimated at 4.6 percentage points for 2008, from 5.1 percentage points for 2007.



ENDNOTES

¹ International Monetary Fund

² Compared to the average of 55 per cent in 2007.

³ Results are obtained from the lending activity survey on the second half of 2008, with credit officers at commercial banks. This survey was conducted in late December and early January 2009.

⁴ Loan repayment period.

⁵ Industrial loan grew on average 47 percent in 2007.

⁶ The same concern appeared also in October, when the overnight interest rate reached the maximum rate of 7.69 percent.

⁷ In November, the Bank of Albania changed the auction form for open market operations to open amount auctions (fixed interest rate, base rate) from the fixed amount ones applied until that moment. Also, in December the overnight loan interest rate dropped by 100 basis points.

⁸ NEER – the nominal effective exchange rate, estimated relative to two major currencies, according to the approximate weight they occupy in the foreign trade - the euro (80 percent) and the usd (20 percent). A higher NEER coefficient implies the lek's appreciation.

⁹ The term "Forward" means a bilateral agreement to carry out a foreign exchange transaction at a specific future date. The exchange rate is fixed at the agreement date and differs from the current exchange rate only by the interest rate spread between both currencies at the specified period.

¹⁰ Great Britain, Irish and Norwegian currencies slid respectively by 17, 14.5 and 14.4 percent.

¹¹ For comparative reasons the data are turned into index base October 1, 2008. Bulgaria and Macedonia are excluded herein, due to implementation of a fixed exchange-rate regime.

¹² The volatility of euro/lek and usd/lek ratios is measured as a monthly standard deviation $[\sum(x_{ti} - x_{ti})^2/n - 1]^{1/2}$, i = euro and dollar relative to the lekun and x_{ti} – at period t , x_{ti} – i period mean.

¹³ Calculated as a spread between weighted interest rates of one-year time deposits in ALL and in Euro.

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CHAPTER IV MONETARY POLICY INSTRUMENTS AND FOREIGN RESERVE MANAGEMENT

4.1 MONETARY POLICY INSTRUMENTS

The main goal in using monetary policy instruments is liquidity management, aiming at orienting the short-term interest rates around the base interest rate signalled by the Bank of Albania. Besides pursuing this goal, the monetary policy instruments are used in view of interbank money market development. In this context, open market operations are oriented towards creating a liquidity structural shortage in the banking system (first nine-month period), aiming at enhancing the monetary policy transmission efficiency, promoting the interbank market activity and at the same time, meeting its net needs.

International confidence crisis at the beginning of the fourth quarter of 2008 triggered deposit withdrawal from commercial banks in Albania, and in consequence, increased the liquidity shortage in the banking system. This was reflected in interest rate rise and slowdown of banks' activity in the money market. In order to facilitate the banking system, the Bank of Albania applied changes to some of its instruments. These measures provided an easing effect, transmitting the message that the Bank of Albania, fulfilling the criteria for risk monitoring, is ready to inject the needed liquidity, in order to normalize the money market situation.

4.1.1 OPEN MARKET OPERATIONS

Open market operations, which consist of the main open market operation, fine-tuning operations and structural operations are core operations for liquidity management by the central bank. The dynamics of 2008 events required the employment of all open market operations.

- *MAIN OPEN MARKET OPERATION*

Repurchase and reverse repurchase agreement of one-week maturity is used as the main instrument of open market operations. During the first quarter of the year, in order to manage the seasonal liquidity balance generated from money return to the system and from budget funds, the Bank of Albania withdrew liquidity through repurchase agreement of one-week maturity, averaging ALL 3.6 billion a week. During the rest of the year the reverse repurchase agreement of one-week maturity was employed, injecting on average ALL 5.8 billion a week.

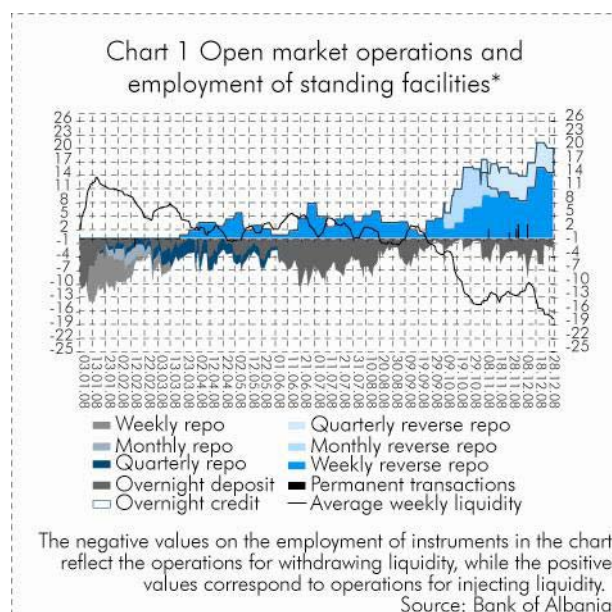
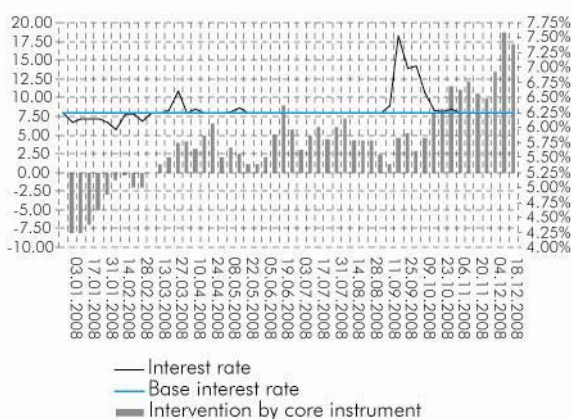


Chart 2 Main operation of the market by auction dates (in ALL billion)



Source: Bank of Albania

In order to enhance the monetary policy effectiveness and interbank market activity, the Bank of Albania operated through variable-price auctions until November. The announced amount was a result of analyses and projection of net liquidity needs of the banking system. Until the end of the first nine-month period, the interest rate of auctions of this type recorded insignificant deviations from the 6.25 percent base rate fixed by the Bank of Albania's Supervisory Council. Consequently, the tension induced in the banking system from deposit withdrawal at the beginning of the last quarter of the year was reflected first of all as a pressure on interest rates of banks' demand for liquidity from the Bank of Albania. Though the announced amount in weekly auctions was sufficient to meet the system's demand for liquidity, the interest rate pressure was

felt for about five weeks on end.

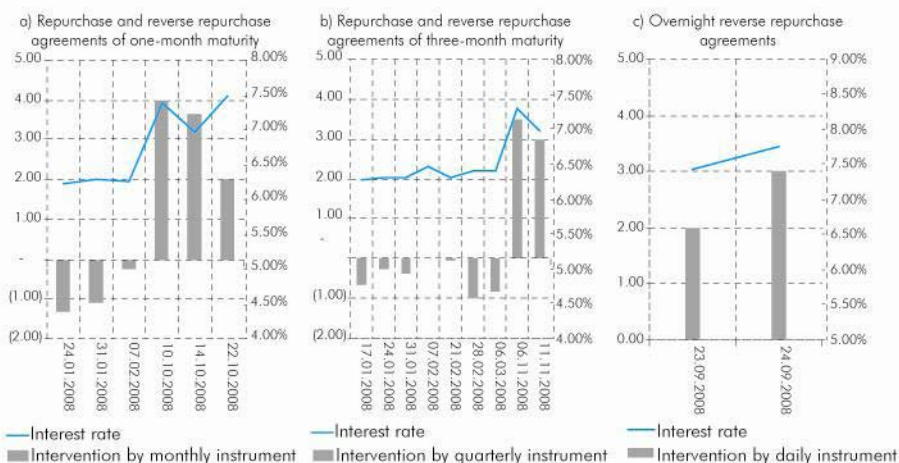
In order to stabilize this tendency, the Bank of Albania changed the form of one-week reverse repurchase agreement auctions in mid-November, injecting liquidity through fixed-price auction – the base rate of the Bank of Albania.

• FINE-TUNING OPERATIONS

In contrast to the main operation, which is executed weekly, the frequency of fine-tuning operations is not standardized. They are used at specific moments, when adjustment of interest rate fluctuations driven by unexpected and/or long-term moves in market liquidity is needed.

In the first quarter of the year, repurchase agreements of one- and three-month maturity were employed, in view of rapid reduction of excess liquidity, in order to minimise the pressures for interest rate cut.

Chart 3 Fine-tuning operations by auction dates (in ALL billion)



Source: Bank of Albania

Repurchase agreements of one-month maturity were used three times, withdrawing on average ALL 0.9 billion, whereas repurchase agreements of three-month maturity were used seven times, withdrawing on average ALL 0.45 billion. Monthly auctions had an average bid/cover ratio¹ of 49.5 percent, whereas the same ratio was lower for three-month auctions, 35.6 percent.

In order to normalise the concern about liquidity shortage triggered by the psychological factor during the last quarter, the Bank of Albania, along with the employment of the main instrument, injected liquidity through reverse repurchase agreements of one-month and three-month maturity. The average injected amount was respectively ALL 3.2 billion in three monthly auctions and in two quarterly auctions. Monthly auctions had an average bid/cover ratio of 95 percent, whereas the same ratio was higher for quarterly auctions, 148 percent.

The low bid/cover ratio in both cases of repurchase agreement auctions indicates a lower effectiveness that the operations have under the conditions of ample liquidity, since participation in them is at banks' discretion. Otherwise, when operating under liquidity shortage, banks depend on the liquidity injected by the Bank of Albania and in consequence, central bank operations determine the interest rate performance.

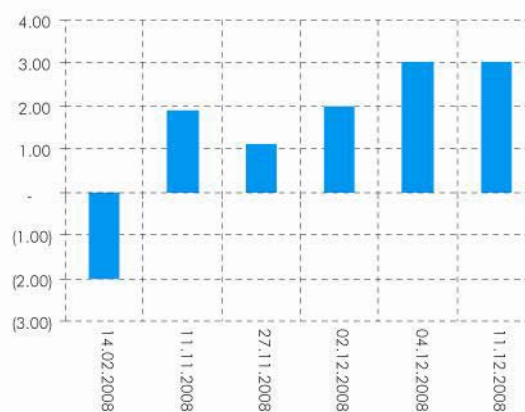
To adjust the liquidity position of the banking system, during the last days of one of reserve requirement maintenance periods (September), the Bank of Albania employed overnight reverse repurchase agreements for two consecutive days, injecting ALL 2.5 billion on average.

- **STRUCTURAL OPERATIONS**

Structural operations are used when long-term liquidity structure adjustment is needed and are conducted through outright purchasing and selling of treasury bills. At the beginning of 2008, in view of orienting operations towards a structural liquidity-absorbing in the banking system, the Bank of Albania decreased its treasury bill portfolio by ALL 2 billion, through one single auction.

Structural operations experienced the reverse side in the last quarter of the year. Considering that deposit withdrawal was not reflecting the quality of a recoverable phenomenon for a short period of time², the Bank of Albania conducted in end-2008, five auctions for outright purchase of treasury bills from second tier banks. On average ALL 2.2 billion treasury bills were purchased in those auctions.

Chart 4 Structural operations by auction dates
(in ALL billion)



Source: Bank of Albania

Box 7. Changes to the operational framework of central banks in adjustment to the market situation

The financial crisis that started in 2007 and upheaved to an economic crisis in 2008 has highlighted the central banks' role in ensuring the macroeconomic and financial stability, besides its classical function of achieving and maintaining price stability. The turbulences put into question the functioning of the financial system and presented challenges to policy-makers and regulatory authorities throughout the world. In this light, central banks have made efforts to address the increased uncertainty, trade volatility and credit risk, taking non-standard measures and cooperating closely with one-another. The measures resulted effective in relaxing the agents, decreasing the perceived risk and rescuing the interbank market, but they have not yet resolved all problems that have accompanied the financial crisis in the real sector. A summary of the reformulation of the Federal Reserve's and the ECB's operational framework and some changes to the monetary policy instruments in the framework of liquidity constraints are presented below:

FEDERAL RESERVE

First, in order to ease the inter-bank market tension, the central banks functioned as lenders of last resort, providing short-term liquidity. Prior to the crisis, the Federal Reserve was restricted in the variety of bank collateral and in the number of partners for loan extension. The accepted collaterals were government securities rated as AAA. The transaction parties were limited to 19 intermediaries (mainly investment banks). Liquidity constraints in the whole financial market segments in 2007 led to changes to the regulatory framework, broadening the type of accepted collateral, the number of transaction partners and the lending term. The latter was extended over a period of 28-35 days, while the counterparty list contained 7000 banks. The credit rate was lowered by 50 basis points and the recipients were anonymous, so as not to cause panic to the market. A swap³ agreement was concluded during this period with the ECB and the SNB⁴ for providing the market with both of these currencies. In September 2008, the lending term was extended to 90 days and swap agreements were concluded even with the central banks of Australia, Sweden, Denmark and Norwegian, and later on with the Bank of England. Until year-end, the Fed introduced some schemes to thaw the money market crunch, launching liquidity against non-traded collaterals, stocks included, or purchasing instruments backed up by mortgage loans. During this period government securities were also sold against debts that were backed on consumer credit and therefore, were considered as of high risk. The use of such loans was extended beyond year 2008 and their maturity varied from 1-3 years.

Along with these measures, since September 2007, the Fed cut consecutively the base interest rate to the last benchmark, close to zero percent.

EUROPEAN CENTRAL BANK

Events occurring over the last two years have presented almost the biggest challenge to the European Central Bank (ECB) and its operational framework in 10 last years (since its creation). At the beginning of the crisis in Europe (in 2007), central bank's role as the lender of last resort was viewed as detached from the monetary policy decision-making role. Though at the beginning the ECB provided liquidity in euro and US dollar (via swap lines with the Fed), it did not operate with the interest rate, regarding this as an instrument for monitoring inflationary pressures. At this time, the ECB did not need to change the regulatory framework, since the existing one contained a relatively wide range of collateral in the counterparty list. This concept of functions division was placated, upon crisis upheaval, ultimately reaching the real economy and lending to the private sector in the third quarter of 2008.

In mid-September 2008, the USA tensions were immediately reflected in the money market in Europe, which more or less, ceased functioning. In consequence, the ECB took a number of corrective measures, some of which were unprecedented. To mitigate the EONIA rate volatility, the ECB narrowed the corridor of standing facilities by 50 basis points (with effect until January 2009). At the same time, it was intervened via open market operations, following a "fixed rate full allotment" tender procedure. Besides weekly operations, there were conducted operations for providing liquidity of 3-6 month maturity. Another exceptional step was the one for refinancing, with a maturity coinciding with the period of holding reserve requirement. At this time, measures were taken to further extend the list of instruments that might be used as collateral in ECB's lending operations. Besides with the Fed, swap lines were established even with National Swiss Bank and auctions were carried out for providing the market with these currencies.

The measures taken by the central banks of both these economies turned out successful in overcoming the interbank market liquidity constraints, but have not yet managed to eliminate uncertainty on lending to the economy.

BANK OF ALBANIA

The international developments dynamics in the last quarter of the year, which was reflected also in the Albanian banking system, in the form of confidence crisis in banking institutions, caused a rapid decline of banking system liquidity. The uncertainty induced from this situation was reflected in the non-smooth operation of money market and in larger risk premiums. In order to normalise the situation created in the banking system, the Bank of Albania applied several changes to its instruments, aiming at facilitating the liquidity injection, but sticking to the criteria for its provision. The changes are presented below, in a chronological way:

1. Expanding securities base, subject to reverse repurchase agreements, including, besides treasury bills, even the bonds issued by the Government of the Republic of Albania, of a residual maturity of not more than 365 days. The inclusion of bonds as subject to reverse repurchase agreements increases the access for getting liquidity at the cost of the base rate of the Bank of Albania, since the bonds might be used only as guarantees for overnight loan and intraday loan extended by the Bank of Albania to second tier banks, upon their request.

2. Expanding the space for using the required reserve, from 20 percent to 40 percent per day: This expansion was aimed at creating a higher flexibility to banks of the system for a more effective administration of sudden liquidity volatility. On the other hand, in the long run, expanding the use of the required reserve would lead to increased interbank money market activity.

3. Temporary passing to an asymmetric corridor, dropping the spread between the base rate of the Bank of Albania and overnight credit, from 175 basis points to 75 basis points. Lowering the overnight credit rate was aimed at reducing the risk from short-term interest rate volatility in cases of sudden liquidity outflow and decreasing the interest rate volatility in the interbank money market.

4.1.2 STANDING FACILITIES

Standing facilities – overnight deposit and overnight loan – are instruments available to commercial banks to manage (temporary) daily liquidity. Theoretically, under the conditions of a regular presence of the central bank

in the market (through its main instrument), a developed interbank market and the opportunity to use the required reserve on a daily basis, the employment of standing facilities by commercial banks should be minimal.

Concretely, both above conditions – the regular presence of the Bank of Albania in the money market and the opportunity to use the required reserve – have been constantly fulfilled over last five years. In the meantime, the relatively low development of the interbank market remains the factor that brought about a large use of overnight deposit in 2008.

The employment of overnight deposit throughout all the business days of 2008 was a result of commercial banks' tendency to hold structural liquidity, which is deposited at a daily maturity with the Bank of Albania, in order to reduce banks' cost. On average daily values, the overnight deposit instrument was employed by ALL 3.6 billion a day in comparison to ALL 1.6 billion a day in 2007. Unlike in 2007, when the Bank of Albania was present in the first half of the year in terms of absorbing liquidity through its main operation (which reduces the use of overnight deposit), during 2008 there was intervened for about ten months in terms of injecting liquidity. The direction of Bank of Albania operations, combined with the low interbank market development has resulted to increased liquidity deposited at an overnight maturity with the Bank of Albania.

On the other hand, the increased structural liquidity of banks, mainly during the first nine-month period of the year, dropped to minimum the employment of overnight loan. Over a twelve-month period, the overnight loan was used in 21 business days, averaging to ALL 0.3 billion. The overnight loan was more concentrated during the last quarter of the year, mainly by small banks of the system, which due to existence of trading limits, faced difficulties in finding liquidity in the interbank market.

4.1.3 ADDITIONAL LIQUIDITY PROVIDING INSTRUMENTS

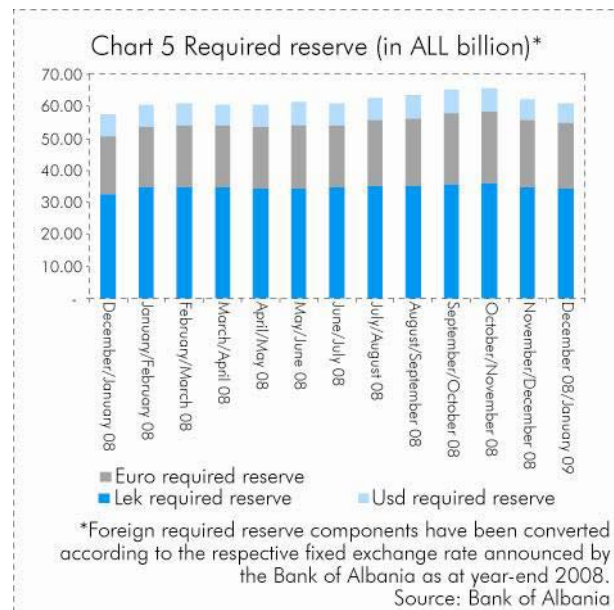
Lombard loan is the last lending instrument of the Bank of Albania used to help banks overcome temporary liquidity shortages, provided they are financially sound. This instrument was not used at all during 2008.

4.1.4 REQUIRED RESERVE

Required reserve is a monetary policy instrument that aims at adjusting the banking system liquidity and stabilizing the interest rates. The required reserve ratio is 10 percent of commercial banks' deposits for 2 years, in the three currencies – the lek, euro and US dollar. Its performance during 2008 reflected that of deposits by respective currencies, with one month lag, since the maintenance period of the required reserve starts on the 24th calendar day of each month and corresponds to deposit position of the preceding calendar month.

Required reserve ratio reflected the seasonal growth of deposits over the first and the third quarters of the year, while it was impacted by deposit decline over the last quarter. The annual required reserve growth resulted to 6.2 percent.

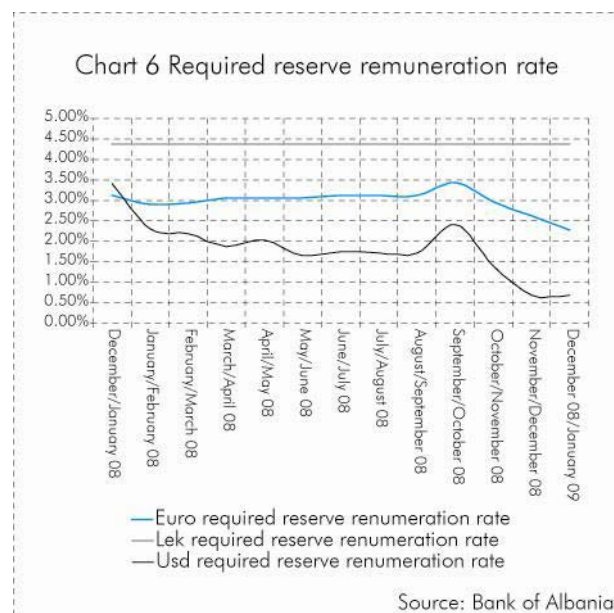
The average weight of ALL required reserve components during 2008 was respectively 56.35 percent, fluctuating from 57.25 percent at year-start to 56.34 percent at year-end. The average weights of foreign exchange required reserve components were respectively 32.57 percent for the Euro required reserve (fluctuating from 31.22 percent at year-start to 33.56 percent at year-end) and 11.08 percent for the US dollar required reserve (fluctuating from 11.53 percent at the year-start to 10.08 percent at the year-end).



During 2008 the opportunity of averaging the ALL required reserve by using 20 percent of it⁵, was efficiently exploited by banks, in order to manage unexpected liquidity fluctuations. This made the deviation of the account position from the required reserve ratio at the end of the maintenance period fall, from on average +0.8 billion leks in 2007 to on average of +0.5 billion leks.

However, the usage of the required reserve for most of banks was restricted only for managing the unexpected liquidity fluctuations and not for active management of liquidity against expectations during the maintenance period. This active management would serve the interbank market development. Increasing the space of required reserve usage from 20 percent to 40 percent in the long run raises the opportunity of active management of reserve within the maintenance period, sustaining the interbank market activity.

Performance of the required reserve remuneration rates has reflected the interest rate performance they derive from.⁶ Concretely, the ALL required reserve remuneration has remained unchanged at 4.375 percent, since the base rate of the Bank of Albania, on which the remuneration rate is calculated for 2008, remained unchanged at 6.25 percent.



The required reserve remuneration rates as at October 2008 were based on the 12-month market rates (Libor and Euribor). Upon entry into force of the reviewed regulation on reserve requirement, the foreign exchange required reserve remuneration is based on respective central banks' base rates – the

European Central Bank and the Federal Reserve of the USA. Interest rate cuts applied at these banks led to decrease of remuneration rate by respectively 83 basis points for the euro required reserve and 270 basis points for the USD required reserve.⁷

4.2 FOREIGN RESERVE MANAGEMENT

Foreign reserve management continued to perform in accordance with the goals and criteria required under the regulatory base, as concerns risk and return on investment. This activity that represents a functional duty of the Monetary Operations Department was enriched during this year with a new service, which is the securities lending. The lending activity helped generating additional income from foreign reserve assets management, without impeding the development of the common activity of management process and observing the restrictions set on the permitted risk level.

One of the highlights in the framework of foreign reserve management is related to the confidence crisis that started in the global financial markets in September. To respond to the situation created upon the onset of this crisis, the Supervisory Council and other structures engaged in reserve management process, made some steps, up to complete reduction of exposure to credit risk. The Bank of Albania is pursuing a conservative policy in reserve funds management, reflected both in the range of instruments allowed for investment and in the restrictions required to be undertaken with regards to risks. In spite of this, under the conditions of unprecedented events of last months of 2008, the restriction of instruments only in instruments issued by the government and government agencies was assessed as the most appropriate solution for the situation. The objective of safety in investing foreign reserve funds represents an objective of primary importance to the management process. This has been reflected in permitting funds investment at financial institutions that have very good qualities, as concerns their reputation in settlement of their liabilities. The experience created during these developments of the crisis has been useful to highlight the importance the tracking of credit risk and investment have in improving the professional qualities of the relevant staff, aiming at the prudential assessment of institutions and financial instruments, in which foreign reserve funds will be invested.

- *STATISTICS ON FOREIGN RESERVE PERFORMANCE OVER 2008*

During 2008 the gross foreign reserve, evaluated and reported in US dollar increased by about USD 205.72 million, to USD 2,344.16 million at end-December.

The main factors impacting on gross reserve are presented in the following:

- A. In relation with the Ministry of Finance, the effect was positive, at USD 26.65 million, according to the following items:

- Privatization receipts, USD 158.83 million;
 - Receipts from loans extended by International Development Agency (IDA) etc., at USD 447.93 million⁸;
 - Transfers, USD 580.11 million.
- B. In relation with commercial banks, the effect was positive, at USD 20.38 million, according to the following items:
- Commercial banks' depositing at the Bank of Albania to fulfil the required reserve and other operations related to their capital, USD 113.25 million;
 - Transfers, USD 92.87 million.
- C. The effect of Bank of Albania's operations was positive, USD 213.92 million, according to the following items:
- inflows from IMF loan disbursing, USD 7.94 million;
 - buying of FX from commercial banks, the Ministry of Finance and other institutions at USD 316.03 million:
 - USD 225.71 million (the banking system),
 - USD 85.86 million (Ministry of Finance),
 - USD 4.46 million (other institutions);
 - Receipts ensured from foreign reserve investment as at end December is estimated at around USD 76.44 million. The re-evaluation effect for the portfolio, due to interest rate fluctuations is estimated to a positive value of USD 48.65 million;
 - Settlement of Bank of Albania's dues to the IMF, USD 15.75 million;
 - Settlement of external debt for the Albanian government, USD 61.87 million;
 - Transfers at about USD 12.07 million;
 - Selling of foreign currency to the Ministry of Finances at USD 145.45 million.

During 2008 the foreign exchange rate volatility of currencies composing the foreign reserve has negatively influenced the gross reserve value, recording an effect of about USD 55.23 million.

ENDNOTES

¹ Cover in this case is the amount announced by the Bank of Albania in respective repurchase agreements, while bid is the demand of banks to participate in those auctions.

² The longest temporary operation available to the Bank of Albania is 3 months.

³ In a broad sense, swap means exchange of investment instruments, payments, liabilities, foreign currency. The agreements concluded between the Fed and the ECB means exchange of foreign currencies, American dollar and euro.

⁴ Swiss National Bank.

⁵ During 2008 the daily space for using the ALL required reserve was 20 percent. The increase of the usage space to 40 percent was approved by the Bank of Albania's Supervisory Council on 11.12.2008, but it entered into force on 24.01.2009, upon the start of the new maintenance period.

⁶ Required reserve remuneration rates are 70 percent of the rate on which they are derived.

⁷ Raising remuneration interest rate of the foreign exchange required reserve, at start of the fourth quarter of the year, reflects the raising of interest rates of the Euribor and the Liborit, due to confidence crisis after the Lehman Brothers' collapse.

⁸ This figure contains also the depositing for the account of the Ministry of Finance of Eur 230 million (credit disbursing for financing the Rrëshen-Kalimash road).

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CHAPTER V FINANCIAL STABILITY AND BANKING SUPERVISION

5.1 BANKING SYSTEM PERFORMANCE

In contrast to the previous year, mixed and unsteady developments occurred during 2008. The banking system analysis reveals an increased risk level and a reduced financial capacity. The first half of the year highlights more positive developments relative to the second one, when especially the last quarter was distinguished for contributing to the worsening of the main banking system indicators. However, the volatility and non-good performance of several main indicators has not put at risk the regulatory capital ratio needed for covering the risks taken by the banking system.

The banking system continues to be engaged mainly in collecting deposits and increasing lending. Though at moderate rates, the system's assets and liabilities grew further in 2008. Exposure to credit risk has also increased, as a reflection of a higher share of loan portfolio to total assets of the system. Furthermore, non-performing loans increased significantly and at accelerated paces, thus affecting the loan portfolio quality. In consequence, the profitability measured by the RoAA deteriorated, due to increased expenses for covering loan losses, which affected the net result of the system. The level of the above-mentioned indicators is not regarded as critical, but the dynamic and intensity of developments requires a more prudential and ongoing monitoring.

The banking system performance in 2008, assessed from the viewpoint of the net result performance, was obviously weaker than in 2007. The net result reflected volatility during 2008. It is estimated at 26.5 percent smaller than in the previous year and reflects mainly the rapid growth of expenses for provisioning, particularly over the second half of the year. Also, operating expenses increased considerably, due to constant expansion of the banking system.

Indicators	December '08	December '07	December '06	December '05
Net result (after tax)	7.33	9.98	7.45	6.60

Source: Bank of Albania

Table 1 Net result in ALL billion

Increased net result from interests and from non-core activities, though at lower pace relative to end-2007, has reflected the growth of higher-interest bearing assets share, as an expression of ongoing orientation of the banking system towards riskier assets and the generally stable growth of the banking activity volume.

Compared to end 2007, the NIM seems almost the same, while its components have increased proportionally. The performance of NIM

indicator during 2008 reveals a slightly downward trend. The NIM peaked by 4.24 percent at end of the first quarter, down to 4.19 percent at end of the second quarter and 4.13 percent respectively for two last quarters. Both its components increased in an ongoing basis and the indicator performance was determined by more accelerated growth of financing cost from banks, mainly public deposits, as a reflection of the orientation to raise the market share on the liability side.

Table 2 Profitability indicators from core activity in percentage (cumulative)

Indicators	December '08	December '07	December'06	December'05
Interest income/average income-bearing assets (1)	8.06	7.26	7.05	6.81
Interest expenses/average income-bearing assets (2)	3.94	3.17	2.83	3.08
Net interest margin (NIM)[(1) – (2)]	4.13	4.09	4.22	3.73

Source: Bank of Albania

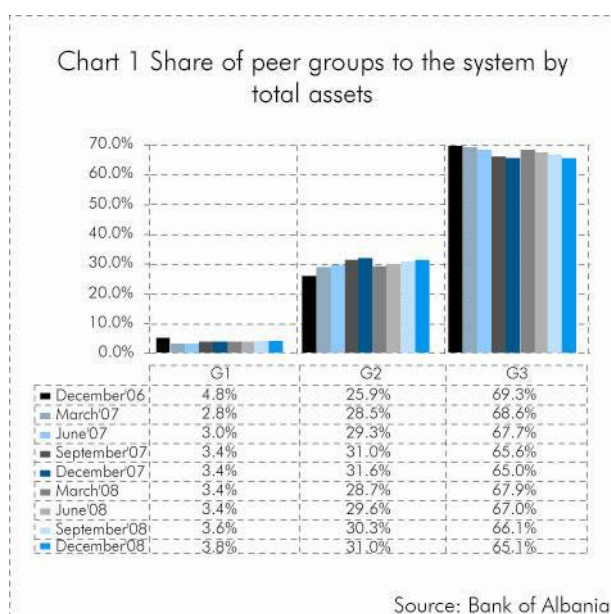
It is worth noting that the RoAA indicator for 2008 never reached the level of 2007. The RoAA for the first quarter of 2008 is estimated at 1.17 percent. It underwent a higher and steadier performance in two following quarters, recording the highest level in the second quarter, about 1.31 percent, being closed at a significantly lower level at the end of 2008. The significant reduction of the RoAA, particularly at end-2008, compared to 2007, derives above all from the significant reduction of the banking system net result.

Table 3 Core profitability indicators in percentage (cumulative)

Indicator	December '08	December '07	December'06	December '05
RoAA	0.91	1.48	1.36	1.40
RoAE	11.35	20.32	20.17	22.24

Source: Bank of Albania

Efficiency indicator is estimated at a higher level for end-2008 relative to 2007, respectively 0.54 against 0.50. It is assessed that this indicator has performed in a balanced way and with components distinguished for a progressive and steady growth.



The banking system presented a growth of total assets, by about ALL 91.8 billion or 12.4 percent, indicating a moderate growth rate for 2008, against the growth by ALL 118.1 billion or about 19 percent in the previous year. In contrast to the panorama of the third quarter, the last quarter of the year presented a decline of total assets of the system by about ALL 23.1 billion or 2.7 percent, determined mainly by large banks of G3 peer group.

Notwithstanding the dynamics of peer bank groups during 2008, which reveals a decreased share of large banks of the system and an increased impact of small-banks and medium-sized ones, the large banks continue to dominate significantly.

The degree of banking system intermediation in the economy and the contribution of lending has increased over years, as an expression of growth of total assets and credit to gross domestic product.

Table 4 Share of total assets and loan portfolio of the banking system to gross domestic product

Indicator	2000	2001	2002	2003	2004	2005	2006	2007	2008
Total assets (in ALL billion)	270.8	318.5	339.3	373.6	426.4	496.6	624.3	742.9	834.1
Total assets /GDP (in %)	50.2	53.5	51.6	50.2	51.9	59.3	69.4	75.9	78.0
Total credit /GDP (in %)	5.3	4.7	5.9	6.8	8.5	15.3	22.0	29.9	37.1

Source: Bank of Albania

Herfindahl index values, calculated for total of assets, deposits and credits respectively, indicate a stable but still far-from-optimum level, though approaching it.

	2002	2003	2004	2005	2006	2007	2008
H index (assets)	0.32	0.30	0.27	0.21	0.18	0.15	0.15
H index (deposits)	0.37	0.35	0.31	0.24	0.20	0.17	0.17
H index (credit)	0.17	0.15	0.11	0.10	0.11	0.11	0.12

Source: Bank of Albania

Table 5 H (Herfindahl) index of asset, deposit and credit concentration

Year 2008 continued to present a credit growth, accounted for about ALL 104.3 billion or 35.7 percent, against the growth by ALL 94.5 billion or 47.7 percent in 2007. In the meantime, the monthly rate of credit growth is presented chaotic, without a clear trend against the average growth of 2.13 accounted for 2008.

Quarterly credit growth	Q. I	Q. II	Q. III	Q. IV
In ALL million	20,870.6	33,510.6	30,796.7	19,137.5
In %	7.1	10.7	8.9	5.1

Source: Bank of Albania

Table 6 Quarterly credit growth over 2008

The fourth quarter of 2008 recorded a rise in non-performing loans by about ALL 10.77 billion or 69.2 percent, compared to the rise by ALL 640.6 million (or 4.3 percent) in the third quarter. During 2008 the increase of non-performing loans accounts for ALL 16.5 billion or 167.6 percent more than at end-2007. The growth paces of non-performing loans are concerning. Under the conditions of a possible containing of total credit outstanding growth, in the coming periods further deterioration of its quality is expected, reflected in the ratio of gross non-performing loans to total gross loans.

Due to several-times-higher growth of non-performing loans to that of total outstanding loans during 2008, a rapid exacerbation of loan portfolio quality indicator (i.e., the non-performing loans to total credit outstanding) was registered, from 3.37 percent at end-2007 to 6.64 percent at end-2008. It is estimated that the indicator level makes up a record figure, the highest in six last years. On net basis, this indicator is estimated at 3.9 percent, being more than twice higher than the level of 1.8 percent at end-2007.

Quality of household and business loan portfolio deteriorated during 2008, particularly during the last quarter of the year. Loan portfolio quality indicator pointed out businesses as more problematic – with about 7.6 percent non-performing loans at end 2008, from 3.6 percent in the previous year. In the mean time, as concerns the households this indicator accounted for about 5.5 percent, from about 3 percent in December '07.

The ALL loan portfolio continues to be more problematic in terms of its quality, with the indicator accounting for 7.5 percent against 6.3 percent of foreign currency one. However, taking into consideration the significantly higher share of foreign currency credit and the worsening pace of its quality indicator¹, the situation is regarded more concerning for foreign currency loans, since the risk and consequences accompanying this portfolio are of a materially higher importance.

During 2008 the banking system was involved in important structural changes, which brought about increased domination of foreign capital of the system. Such structural changes and addition of paid-in capital² by banks during 2008, led to increase of foreign capital by ALL 12.5 billion (33 percent) and decrease of Albanian capital by ALL 266 million (5.6 percent). As at end December 2008, the foreign capital of the system was ALL 50.3 billion or 91.8 percent (from 88.8 percent in the previous year), while the domestic capital was ALL 4.5 billion or 8.2 percent.

At end 2008 the shareholders' equity of the system accounted for ALL 71.5 billion. During this year its growth was ALL 15.4 billion (27.5 percent), against ALL 14.5 billion (34.3 percent) in 2007. The paid-in capital continues to be the most important element of the shareholders' equity. During 2008 the paid-in capital of the system amounted to ALL 51.1 billion or 24.3 percent, up from ALL 41.1 billion. The worsening of the banking system performance during 2008 has made the net result of the system impact by ALL 2.6 billion less to total shareholders' equity of the system.

The ratio of assets to shareholders' equity of the system or otherwise referred to as the financial leverage of the system decreased gradually during 2008. The fall of financial leverage from 13.1 to 1.7 during one year implies that the system is backed less on debt for assets financing. This level is assessed as better than the level of the financial leverage of Europe, USA and Canada. The decreased level of the financial leverage of the system was influenced by G3 peer group.

Total regulatory capital of the banking system is reported at ALL 58.6 billion as at end-September 2008. Compared to the preceding quarter, its value increased by ALL 214 million (0.37 percent), whereas compared to the previous year, it increased by ALL 12.4 billion (26.9 percent). Base capital continued to dominate on the composition of the regulatory capital of the system, accounting for 94.6 percent, from 93.7 percent in the previous year. This indicates a qualitatively good and stable regulatory capital.

	December '06	December '07	December '08
Net non-performing loans/regulatory capital	6.8	9.9	21.7

Source: Bank of Albania

Table 7 Performance of net non-performing loans to regulatory capital (in percentage)

The share of net non-performing loans to regulatory capital of the system was 21.7 percent as at end-December 2008, from 9.9 percent at end-December 2007 and 11.4 percent at end of the previous quarter. The annual rise of the indicator is due to a faster growth of net non-performing loans than that of the regulatory capital, mainly 193.7 percent against only 26.9 percent. Therefore, the system's ability to cover possible loan losses with regulatory capital results significantly lower during a year.

Due to increase of the system's regulatory capital at considerable paces (29.6 percent) and of the total assets and risk-rated off-balance sheet items (25.8 percent) during 2008, the system's capital adequacy ratio is estimated at 17.2 percent. This level accounts for 0.1 percentage point more than in the previous year and 0.3 percentage point less than in the preceding quarter.

During the first quarter of 2008, the indicator was upward, to find again the downward trend in the fourth quarter. The decline of the indicator in the fourth quarter was influenced by the application of new rules in risk-rating assets.

Adequacy indicator continues to display higher levels in the small banks of G1 peer group, around 30.8 percent. Both other peer groups indicate lower values. The G1 indicator's value, after the dropping by 9 percentage points in the second quarter of 2008, has consolidated this trend even during the following quarters, whereas for two other groups this rate is variable in time.

Capital adequacy ratio in %	G1	G2	G3	System
December 2008	30.8	15.3	16.6	17.2
December 2007	45.1	15.8	15.5	17.1
December 2006	41.3	15.9	16.0	18.0
December 2005	35.0	19.4	14.4	18.6

Source: Bank of Albania

Table 8 Performance of capital adequacy ratio by peer groups

The banking system presented a satisfactory position of liquidity until end-September 2008. The following months were characterised by a reduction of deposits base in most banks of the system. This phenomenon affected the exacerbation of the liquidity position, being reflected in dropping of liquid assets of the system, deepening of liquidity gap, increasing of credit/deposit ratio, and restricting of the system's possibilities to cover a massive deposit withdrawal in the future.

The total of liquid assets in years, excluding the last quarter of 2008, has been increasing but at low rates, whereas its share to total assets has reflected an obvious downswing. The downward trend of this indicator is a natural outcome of developments occurring in the banking system in recent years, passing gradually from investments in low-risk liquid assets towards investments in long-term riskier and higher-interest earning assets, such as

loans. In 2003 liquid assets accounted for 73.6 percent of total assets; this share dropped to 49.8 percent in 2007 and 42.8 percent in 2008.

Loans received from parent banks, from other banks of the group or from other non-resident institutions are an important source of financing for some subsidiaries or branches of foreign banks in Albania. During the latest years, this source of financing has been expanding. At end 2005, foreign funds constituted only 2 percent of total liabilities of the system, whereas at end December this share increased to 8.6 percent.

“Credit to total deposits” is another important indicator, which helps displaying a complete view of the banking system’s liquidity position. The indicator worsened during the fourth quarter of the year, accounting for 60 percent. The rise of this indicator was caused by an obvious decline of customer deposits, whereas credit continued to grow even during the fourth quarter of the year (increased by 5.1 percent).

Table 9 Performance of credit to deposits indicator in percentage

	Lek	Euro	Usd	All the currencies
2006	17	98	36	38
2007	22	97	34	46
2008	30	112	34	62

Source: Bank of Albania

5.2 LICENSING AND THE REGULATORY FRAMEWORK

5.2.1 LICENSING

During 2008 the licensing process, being part of the banking supervision, consisted in:

CHANGES TO BANK OWNERSHIP STRUCTURE

During the past year qualitative and quantitative changes of bank shareholders’ equity were noted. Qualitative changes consist in increased share of foreign capital in bank shareholders’ equity. Quantitative changes are evidenced in the increased amount of subscribed and paid-in capital of banks. The entry into the Albanian market of entities and banks with experience in foreign markets is assessed to positively affect the Albanian banking system’s development, bringing not only capital but also expertise in terms of banking risk management and administration.

Concretely, during 2008, there was adopted:

- Acquisition of 12.5 percent of the shareholders’ equity of the Union Bank Jnt. Stk., by the European Bank for Reconstruction and Development;
- Transfer of ownership for 76.83 percent of voting stocks of the shareholding of the Italian Development Bank Jnt. Stk., from the existing shareholders to the Veneto Banca Holding S.c.p.A., Italy.

In all transfers of bank stocks adopted, there is noted an upward trend of the share of foreign capital, from the viewpoint of origin. On the other hand, there is noted the entry of internationally experienced entities and banks, which is expected to positively influence the Albanian banking system development.

BANK LICENCE REVOKING AND MERGERS

In 2007 the merger of the Italian Albanian Bank with the American Bank of Albania was carried out. This new phenomenon was associated with the application of new licensing practices, unknown or not applied previously. Following this practice, in 2008 the licence of the Italian Albanian Bank was revoked. Its activity was transferred to the American Bank of Albania. The Bank of Albania adopted in 2008 the change of the name of the American Bank of Albania into Intesa Sanpaolo Bank Albania.

Also, completing the transformation process of the First Investment Bank-Tirana Branch and licensing the First Investment Bank Albania, the Bank of Albania's Supervisory Council decided on revoking the licence of the First Investment Bank – Tirana Branch.

It is worth noting that the revoking of both bank licences was not carried out because of any failure in their activity, but it is related to the transformation taking place in the Albanian banking system.

As at end 2008 there are operating 16 banks in the Republic of Albania, of which 14 are banks and 2 are branches of foreign banks. There was not submitted any new application for a bank licence throughout the past year.

ACTIVITY ADDED IN THE LICENCE ANNEX

Banking activity expansion was another feature of the banking sector's developments over 2008, adding the permitted activities or banking products. Thus, approval was granted on adding factoring activity and trading transaction financing to the list of activities specified at the licence annex of the Credins Bank. Also, 8 new cases of e-banking products were adopted, consisting in implementing internet banking product and electronic cards of the ATMs.

BANKS' NETWORK EXPANSION

The rapid network expansion of bank branches and agencies in Albania continues also in 2008. Concretely, 113 branches and agencies were approved and commenced activity in 2008. At the year-end the overall number of branches and agencies amounted to 517, from 404 in 2007.

Table 10 Indicators of banks' network extension as at end 2007

No.	Banks	No. of branches at home	No. of agencies	No. of branches abroad
1	Raiffeisen Bank	98		
2	National Commercial Bank	21	20	1
3	United Bank of Albania	3	1	
4	Italian Albanian Bank (Banca Italo-Albanese)		7	
5	Italian Development Bank (Banca Italiana di Zviluppo)	4		
6	Tirana Bank	39	4	
7	National Bank of Greece - Albania Branch	5	19	
8	International Commercial Bank	5		
9	Alpha Bank -Albania branch	23	1	
10	American Bank of Albania	8	15	4
11	ProCredit Bank	24	1	
12	First Investment Bank – Albania Branch ³	-	-	
13	Emporiki Bank	4	7	
14	Credit Bank of Albania	2	1	
15	Credins Bank	21	4	
16	Popular Bank (Banka Popullore)	33		
17	Union Bank	12	12	
18	First Investment Bank	4	1	
	TOTAL	306	93	5

Source: Bank of Albania

Table 11 Indicators of banks' network extension as at end 2008

No.	Banks	No. of branches at home	No. of agencies	No. of branches abroad	Nr. of branches and agencies
1	Raiffeisen Bank	101			101
2	National Commercial Bank	26	29	2	57
3	United Bank of Albania	4	2		6
4	Italian Development Bank (Banca Italiana di Zviluppo)	7			7
5	Tirana Bank	43	4		47
6	National Bank of Greece – Albania Branch	5	25		30
7	International Commercial Bank	8			8
8	Alpha Bank – Albania Branch	48	1		49
9	Intesa Sanpaolo Bank Albania	18	16	4	38
10	ProCredit Bank	29	13		42
11	Emporiki Bank	10	10		20
12	Credit Bank of Albania	2	1		3
13	Credins Bank	23	6		29
14	Banka Popullore (Popular Bank)	39			39
15	Union Bank	15	16		31
16	First Investment Bank	6	4		10
	TOTAL	384	127	6	517

Source: Bank of Albania

APPROVAL OF ADMINISTRATORS

In 2008 the banks submitted 60 requests for approval of administrators appointed by them, under the requirement of the Law "On Banks in the Republic of Albania". The Bank of Albania granted the preliminary consent for those requests. The submitted requests for the preliminary consent of administrators consisted in:

- Appointing administrators for the effect of various movements, depending on bank organisational structure, parallel movements or new appointments;

- Creating new positions for the effect of establishing new structures in banks, for example, risk analysis units;
- Making new appointments, as an outcome of new shareholders' representatives nominated to bank management.

In the approved cases of bank administrators, 10 of them are for the Steering Council of the bank, 12 are Audit Committee members, 6 are Executive/General Director, 30 are department/division/directorate heads, and 2 are directors of internal audit units.

DIFFERENT APPROVALS ON BANK STATUTES

Pursuant to Article 24 of the Law "On Banks in the Republic of Albania", the Bank of Albania shall grant the preliminary consent, inter alia, even to banks' statute changes. Pursuant to this requirement, 6 banks submitted requests for consent to changes to their statutes.

The submitted changes to bank statutes related to the application of legal requirements under the laws "On Banks in the Republic of Albania", "On Trade Associations" and "On National Registration Centre".

CREATION OF NON-BANK FINANCIAL INSTITUTIONS

In 2008 the Fondi Besa joint-stock company was granted a licence, No. 10, dated 26.12.2008, as a non-bank entity for carrying out financial activity pursuant to the banking law. Seven non-bank financial entities were conducting financial activity as at end 2008. Concretely, 4 non-bank entities carry out lending activity, 5 non-bank entities make payments and receivables, 4 non-bank entities perform the intermediation activity in monetary transactions, 5 entities perform financial consultancy and agent's activity, 3 entities offer guarantees (different from banking guarantees), 1 entity carries out financial leasing and 1 entity accepts and manages payment instruments.

GRANTING AND REVOKING A LICENCE TO/FROM FOREIGN EXCHANGE BUREAUS

During 2008 the Bank of Albania granted a licence to 81 foreign exchange bureaus and revoked a licence, upon their request, from 4 foreign exchange bureaus. Also, due to changes in the Regulation "On licensing, organisation, activity and surveillance of foreign exchange bureaus", additional activity was approved for 38 foreign exchange bureaus operating as an agent for money transfer for the account of a non-bank entity (Financial Union of Tirana or Ak – Invest). As at end 2008 there were operating 189 foreign exchange bureaus.

GRANTING AND REVOKING A LICENCE TO/FROM THE SAVINGS AND LOAN ASSOCIATIONS

During 2008 nine new savings and loan associations were licensed and 6

others were revoked a licence as a result of merging with an existing association. Consolidation of savings-loan associations continued even during 2008 and as a result the number of these associations reached 133 at year-end.

Table 12 List of entities licensed by the Bank of Albania from 2000 to end-2008

No.	Entities	2000	2001	2002	2003	2004	2005	2006	2007	2008
1	Banks and branches of foreign banks	13	13	14	15	16	17	17	18	16
2	Non-bank financial entities	2	4	5	7	7	7	6	6	7
3	Foreign exchange bureaus	19	38	58	58	54	58	60	112	189
4	Savings-loan associations			113	131	130	131	125	130	133
5	Unions of savings-loan associations			2	2	2	2	2	2	2

Source: Bank of Albania

5.2.2 REGULATORY FRAMEWORK

The Law “On Banks in the Republic of Albania” and the implementation of Bank of Albania’s mid-term and long-term strategy created the incentive for reviewing the supervisory regulatory framework even during 2008.

Year 2008 finalized the drafting of some new regulations and acknowledged amendments to some other banking supervision regulations.

The following new regulation of importance to the banking supervision were adopted along the year:

- Regulation “On managing the risk from large exposure of banks”, which harmonises the new requirements of the banking law with the entirety of rules and criteria of the supervisory authority on calculating, supervising and reporting large bank exposure to a person/client or a group of persons/clients connected to or in a specific relationship with the bank, aiming at managing the risk deriving from concentrated exposure to them.
- Regulation “On internal audit system at banks and branches of foreign banks” which determines the supervision authority’s rules on internal audit, as part of the responsible governance of banks, aiming at promoting an adequate internal audit system, as an important factor in management and administration of banks and branches of foreign banks.
- Regulation “On transparency about financial and banking services and products”, which focuses mainly on regulatory requirements about the manner and form of providing clients with information on banking products and services, specific publication of effective loan/deposit interest rates, the calculation method of effective interest rate on loans, credit and deposit contract elements, marketing of products and services, protection of confidentiality on client’s information, addressing of complaints of the latter as well as establishment of specific structures (functions) related to those complaints, etc.
- Regulation “On minimum requirements for disclosure of information from banks and branches of foreign banks” which has in focus the

regulatory requirements of the supervisory authority for the disclosure of information from banks and branches of foreign banks to the public and market participants, related to several categories (core operation of the bank, its overall governance and management, its financial performance, its financial position, risk management strategies and practices, exposure to risks and accounting policies).

- Regulation "On minimum technical and security conditions of work premises at entities licensed by the Bank of Albania", which specifies the minimum requirements on technical and security conditions of entities licensed by the Bank of Albania for the conduct of financial and banking business, aiming at smooth and safe operation of their activity.
- Some important changes were made to the regulations "On credit risk management", "On reporting the capital adequacy" and "On risk management in the activity of branches of foreign banks", which relate to credit risk management of banks and branches of foreign banks and serve the ongoing strengthening of measures taken by the supervisory authority on minimizing the banking system credit risk.
- Also some changes were made to the Regulation "On managing the risk from large exposure of banks", triggered by current problems appearing in the global financial system, intended to buffer out the spillovers to the Albanian banking system. These changes consist mainly in putting more prudential thresholds on large exposure indicators and the technique of calculating and recognizing the collateral specified under the regulation, aiming at diversifying the risk from bank concentration in investing in international financial markets.

5.3 ON-SITE SUPERVISION

UNIT FUNCTIONING

On-site inspection office is responsible for evaluating banks' assets and for checking their observance of the legal and regulatory framework. The realised work was based on guaranteeing the development of a sound financial activity. The work is based on the criteria specified by the Supervisory Council, defined by the operational policy of supervision. Being an important link for meeting Bank of Albania's mission, it has fulfilled its obligations by adhering to supervisory principles, making them clear, elaborating and observing them. Intensive work and ongoing prudence have made it an important link to preserve the financial stability.

A feature of activity carried out during 2008 is the commitment to profound analysis of activity of the licensed entities, especially of banking operators. This phenomenon was associated with full evidencing of some problems and engaging of intensive and extensive human resources. Following the set-up practices, the scope of work had in focus preventing the deficiencies rather than dealing with them after their appearance. To this end, possible impacts of certain risk positions were taken into consideration and awareness of certain phenomena was made, intending the taking of due measures.

Besides the observance of the supervisory cycle, a constant contact was kept with banks, in order to timely draw their attention to supervision-related concerns along the year. Efforts were made to take measures, to timely address such issues as loan portfolio quality, applied interest rates and liquidity management.

Complaints made by clients were dealt with throughout the year. Their number, though modest, is increasing compared to the past and the nature of problems is an indicator of an upward public awareness of the banking services, which raises the need for a constant attention to address the problems in due time.

COOPERATION WITH OTHER AUTHORITIES

Taking into consideration financial market developments, particularly over the last months of the year and the importance of foreign capital banks, attention is paid to cooperating with other supervisory authorities. This cooperation has taken place mainly with home countries of banks operating in Albania and with those of the region.

Further to multi-lateral cooperation agreement signed with six region countries, aiming at promoting a structured cooperation in the banking supervision area, information was exchanged about the supervisory features of each country and steps were made for further enhancing the cooperation.

Hence, the cooperation has been strengthened with the Bank of Greece, the country's supervisory authority of the banking system, by exchanging experience and information and the participation of this authority in auditing the expansion of Greek banks operating in Albania.

A close cooperation took place with the General Directorate of Money Laundering Prevention. There has been ensured a constant participation, in the framework of a twining project of this institution with the German counterparty, financed by the European community.

There was intensified the exchange of information and was coordinated the activity with the Deposit Insurance Agency, particularly in late 2008, in the framework of managing the liquidity position of banks.

During 2008, the following examinations were carried out:

Banks	12 full-scope examinations
Non-bank financial institutions	1 full-scope examination
Savings-loan associations	1 full-scope examination
Foreign exchange bureaus	34 examinations
Physical premises of branches of banks and foreign exchange bureaus	201 examinations

Source: Bank of Albania

FINDINGS FROM EXAMINATIONS

- **Banks**

The banking activity underwent various developments during 2008. The first 9-month period witnessed a constant development of activity, increased volume of work, of banking services, of lending to the economy and a larger expansion of the banks' network. This phenomenon was a follow-up of constant developments of banks in the recent years. The competition is enhanced significantly, reflected in the types of the supplied products and their prices. These developments have drawn the supervision's attention to prudentially follow-up the financial performance, the quality of decisions made and their consequences.

The second part of the year underwent an overall shrinkage of the banking activity, affected by the global financial crisis. But, unlike other countries, where the internal developments had stimulated it, the problems appearing in the Albanian banking system were triggered by customer deposit withdrawal because of lack of confidence. This lack of confidence was influenced by information coming from international markets and from informal noise circulating in the country. The contraction is evidenced with a significant decline of customer deposits, particularly of household time deposits. In the wake of these events and the envisages for a downturn of the economic growth of the country in the course of 2009, the banks have reviewed their strategic plans, providing a more conservative approach related to expansion of their activity. The market developments, businesses and consumer behaviour, domestic liquidity position and the economic developments affecting the parent banks in their home countries, are the main factors giving shape to the 2009 prospects. However, developments over the last months of 2008 revealed that the banking system is sound and liquid, withstanding even tough situations of upward request for funds withdrawal.

Concerning the situation of the last quarter of 2008, the banking system developments were attended intensively. Therefore, there was required a daily reporting on customer deposit withdrawal and on some specific balance sheet items that relate directly to the facing of this phenomenon. An appropriate database was set up, processing the data in order to prepare informative and analytical materials on the system's developments week by week. Furthermore, a constant contact was kept with every bank, receiving real time information on the routine performance of activity or certain developments that have become a cause of concern to supervision.

The development of risk management function was held under special attention of banks. This was done depending on the size of banks and type of risk taken. Specific units have been set up in several banks, dealing with risk analysis, whereas some others have opened job positions for this purpose.

The deficiencies observed during on-site examinations are summarised in the adjustment of structures to bank's development, signifying the establishment

of new units, delegation of work powers, and support to them through work operating policies and procedures. There are evidenced some deficiencies in internal audit systems, highlighting the need for improving the quality of work, covering the entire activity and attending and addressing the problems. An ongoing prior attention was shown to management structures, in terms of insufficient operation, for the well-operation of organisational units or establishment and stabilization of some structures when necessary. Special importance was attached to the quality of work for risk management.

On-site supervision has paid special attention to the capitalization level of banks. Besides the analysis of this position, rigorous observance of regulatory thresholds and forecasting of the needs for capital and resources were required. Expansion of clientele base in terms of obligations and lending relations was required, to reduce the concentration risk. Credit risk diversification in various branches of economy was also part of issued recommendations. Special attention was shown to the maintaining of a good liquidity position of banks, its proper management and provision of funds necessary for coping with difficult situations. Because of some inaccuracies found in monthly data reporting, banks were recommended to take due measures to prevent the problem and increase the monitoring on accuracy of dispatched data.

PROBLEMS RELATED TO IMPLEMENTATION OF REGULATIONS

Generally, good observance of the regulatory framework was noted. Nevertheless, they were noted cases of non-material impact on risk exposure situation.

Violations were noted mostly in conjugation with the non-observance of:

- a) The banking law: The breaking of this law has to do with the exposure to connected persons. Such breaking is noted at the moment a decision to extend a loan is made, because of non –accurate evidencing of the connected business groups.
- b) Regulation “On credit risk management”: The level of risk from borrowers has been dealt with constantly and in some cases the incorrect observance of this regulation has been noted, particularly as concerns the credit rating and the provisioning level. The completion of documentation in accordance with this regulation has been a constant requirement.
- c) Regulation “On open foreign exchange positions”. Some sporadic cases of non-observance of this regulation were pointed out; however, they were temporary situations that improved within a short period of time.
- d) Regulation “On capital adequacy”. Non-observance was mainly of a technical nature or an issue of interpretation of the requirements of this regulation.
- e) Regulation “On significant exposures”. There is noted a non-reporting or inaccurate reporting of bank exposures, due to regulatory changes made along the year; however, they have been improved on an

- ongoing basis.
- f) Regulation "On foreign exchange operations". Remarks on the application of this regulation arise mainly in relation to transfers or additional documentation.
 - g) Regulation "On money laundering prevention". Deficiencies relate to prevention of suspicious transactions, establishment and observance of structures, staff training and establishment of a database, reporting of suspicious transactions and meeting of requirements under the new law effected in 2008.
 - h) Regulation "On using the information and communication technology at entities licensed by the Bank of Albania". Breaching of this regulation occurred relatively more frequently, indicating the need for larger investment of banks in improving the information and technology systems. These improvements should be done in terms of assessing the systems, guaranteeing the physical security, drafting an operation plan, documenting the activity, making a disaster recovery plan. Also, the auditing on communication and information technology systems by specialised companies was constantly recommended.
 - i) Regulation "On supervising the electronic banking transactions". Deficiencies related to this regulation have to do with the completion of appropriate documentation and the delivery term to the Bank of Albania. The application of this Regulation was significantly meliorated during 2008.
 - j) Guideline "On transparency of banking operations and services". Non-observance of this Guideline has to do with disclosure of information to the client about changes to working conditions in terms of contract observance, publication of the reference interest rate, notification of the client on all expenses related to the loan, explicit specification of the contract type in the respective contracts, penalties they are exposed to, full publication of information on loans, etc. During the examinations, emphasis was laid on notification of clients on risks they are exposed to during the loan repayment period.
 - k) Bank accounting manual. One of the most evident problems was the classification of investments in securities according to specifications under the manual. Inaccurate classification has brought about the appearance of lower costs for banks.

- **Financial Entities**

This group incorporates two types of entities, non-bank financial institutions and savings and loan associations. While the first can not collect deposits from the public, the second may collect deposits as stipulated under the respective law.

Most frequent problems noted during the examinations relate to the inaccurate calculation and non-observance of prudential standards specified under relevant regulations. These prudential standards relate mainly to risk level.

During the examinations on entities, much importance was laid on improvement of domestic structures, either from the organisational viewpoint or from the regulatory one, in order to prevent any possible frauds. To this end, of importance was the requirement for improving the internal audit system and the work of internal audit unit. Improvement of the lending process was constantly requested, starting from the analysis of borrowing abilities to the accurate classification of the loan portfolio, pursuant to the Regulation "On credit risk management".

Based on the deficiencies found, there was recommended the drafting of realistic and feasible development plans, the functioning of all structures on the basis of internal regulatory framework, investment in information technology systems and observance of the requirements under the regulations on communication and information technology system, creating the necessary security for the smooth operation of activity.

- **Foreign exchange bureaus**

There are carried out 34 examinations over these entities. Deficiencies in their work are recurrent and consist in lack of reporting or data inaccuracy; non-provision of exchange invoices to clients; lack of book-entries or deficiencies in documentation as required under the regulation on their operation.

5.4 CREDIT REGISTRY

The operation of Credit Registry is regarded as an important element for guaranteeing the banking system stability. The Credit Registry constitutes the electronic identifying data base and particularly data on loans, individuals, trading natural and legal persons that have received a bank loan at bank and/or a branch of a foreign bank licensed by the Bank of Albania. Credit registry has two main purposes:

- Assessing and minimizing the credit risk the banking system is faced with, enhancing the possibilities for carrying out sound lending operations;
- Improving and strengthening risk-based supervision.

Credit registry started to operate live on 3 January 2008. From that time on, the credit registry has provided commercial banks with necessary information, so as to judge fairly and rapidly on loan applicant's creditworthiness, thus increasing the possibilities for a sound lending process.

Priorities of the Credit Registry Bureau during the first year of its operation were: constant monitoring of banks' reporting to the Credit Registry, to ensure completion and accuracy of data contained in the Credit Registry Office; monitoring of the use of Credit Registry data by second tier banks; addressing of individual applications of borrowers for receiving a loan report; the project for incorporating micro-finance institutions to the Credit Registry, etc.

DATA REPORTING

All banking system loans, irrespective of their value, are reported to the Credit Registry. In this framework, banks are required to report to the Credit Registry about each new credit extended, new credit disbursement, repaid credit and extinguished credit, data on connected persons and collaterals supporting them, within the next business day; as well as updating of the loan portfolio and respective classification within 15 days of the following month.

CONFIDENTIALITY AND TRANSPARENCY

Information contained in the database is protected and used in accordance with the requirements under the Law "On protection of personal data" and other effective laws and regulations. At any case, in order to avoid misinterpretation of information found in the Registry and to enhance the transparency, the borrowers are allowed to address the Bank of Albania through a clear and specified procedure, for verifying the information about them in the register, as well as for requesting necessary changes.

Also, for a higher transparency, the whole relevant information on the Credit Registry is provided at Bank of Albania's web-site: 'www.bankofalbania.org'.

INCORPORATING MICRO-FINANCE INSTITUTIONS AND NON-BANK ENTITIES IN THE CREDIT REGISTRY

Credit Registry is aimed at containing data obtained from all financial institutions licensed by the Bank of Albania to conduct lending activity. In this framework, during 2008 the Bank of Albania was engaged in drafting and attending the project for incorporating as data users and reporters even the micro-finance institutions and non-bank financial entities licensed for lending activity. The project was designed and is being implemented in some stages. During the first stage, there were introduced: the project, the legal and technical requirements, the information technology infrastructure and the lending database of these institutions. The second stage aimed at assessing the capacities of institutions for meeting the requirements and their willingness to enter the Credit Registry System. The third stage, which will be finalised during the current year, aims at incorporating institutions in the Credit Registry and ensuring the credibility of this process.

INFORMATION AVAILABLE FROM THE CREDIT REGISTRY

During 2008 the Credit Registry was used mainly in banks' service, raising their opportunities for carrying out safe lending transactions and served as an additional instrument to their credit risk management. Concretely, the Credit Registry provides commercial banks with the necessary information, to rightly and rapidly judge on the financial settlement ability and reliability of the loan applicant, shortening the decision-making time for extending a loan, impacting on loan quality rise and cost cut.

The Credit Registry system usually provides a broad level of products, serving the accomplishment of Bank of Albania's functions. The reports produced by the Credit Registry aim at supporting the supervisory mission of the Bank of Albania for improving the assessment of credit risk management, monitoring the non-performing loans level, assessing the loan portfolio quality, evidencing the credit concentration by banks and economy sectors, assessing in detail the type of eligible collateral and guarantees, evidencing the relations among different borrowing subjects, etc. A part of reports serves also for monitoring the effectiveness of Credit Registry operation, in conjugation with the usage of Credit Registry information by banks. These reports are an efficient and fast instrument, since they are provided in real time and help rapid orientation towards the banking system tendencies.

ENDNOTES

¹ Only during the last quarter, the foreign currency credit quality indicator increased by 2.72 percentage points against the growth of 1.91 percentage point for that of lek-denominated credit.

² Paid-in capital includes the capital endowed for branches of foreign banks, as well as the issuing premia.

³ In 2007 the activity of the branch of First Investment Bank was transferred to First Investment Bank Jnt. Stk., the activity of branches and agencies included. This transfer was finalised with the revoking of the licence of the branch of First Investment Bank, with decision No. 28, dated 09.04.2008 of the Bank of Albania's Supervisory Council.

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CHAPTER VI OTHER ACTIVITIES OF THE BANK OF ALBANIA

6.1 PAYMENT SYSTEM DEVELOPMENTS

During 2008 Bank of Albania's payment systems reflected security and efficiency, which are indispensable features for a smooth operation of the payment system. Clearing and payments settlement through banks, in the national currency, is carried out through two payment systems: "The real time gross settlement system - AIPS" and "The automated electronic clearing house system - AECH", in accordance with the interbank payment settlement rules. The real time gross settlement system (AIPS) was accessed by participants to 99.88 percent of its operating schedule. In other words, during 246 business days the system was unavailable for only 2 hours and 22 minutes, due to technical and/or communication problems with the SWIFT.

6.1.1 REAL TIME GROSS SETTLEMENT SYSTEM - AIPS

A total of 56,717 transactions were processed and settled in the AIPS system during 2008, with an average value per settled transaction by ALL 91 million. Relative to 2007, the payments volume settled in 2008 increased 25 percent, while the settled transactions value increased 37 percent.

AIPS system	2006	2007	2008
Transactions number	38,793	45,480	56,717
Transactions value (ALL billion)	3,376	3,745	5,146
Average value per transaction (ALL million)	87	82	91

Source: Bank of Albania

Table 1 AIPS Transactions made during 2006-2008

The greatest number of settled transactions was concentrated in the second quarter of the year, while the largest liquidity circulation occurred in the third quarter of 2008.

AIPS system	Quarter				Year
	I	II	III	IV	2008
Number of transactions	12,845	15,147	14,005	14,720	56,717
Transactions value (ALL billion)	1,047	1,237	1,576	1,286	5,146
Average value/transaction (ALL mln)	82	82	113	90	91

Source: Bank of Albania

Table 2 Distribution of transactions through AIPS by quarters of 2008

About 231 transactions were processed and settled on average per day through AIPS, with an average daily circulation of ALL 21 billion. The total value of liquidity circulated through the AIPS during 2008 is estimated at about 5 times Gross Domestic Product for the year¹. Currently, all the banks operating in Albania are direct participants for settlements through the AIPS.

In a more detailed way, the types of transactions processed and settled through the AIPS during 2008 and their relative share to the total is presented in the following table:

Table 3 Types of transactions through the AIPS

Type of transactions through AIPS	Number of transactions	Volume		Value (ALL billion)	
		Relative weight	Absolute value	Relative weight	
BoA financial transactions/instruments	4,364	8%	3,053.2	59%	
Cash transfers to/from the issue	9,052	16%	249.3	5%	
Inter-bank payments	8,512	15%	833.8	16%	
Customer payments	29,068	51%	484.9	9%	
Settlements for net clearing systems	5,721	10%	524.7	10%	
Total	56,717	100%	5,146	100%	

Source: Bank of Albania

Out of total transactions processed and settled through the AIPS during 2008, we note that customer payments that the banks settled among themselves account for about 51 percent to the total, including here the payments the banks post daily to the government budget account, for the account of their clients. Concerning the transactions value, the highest circulation of liquidity, about 59 percent to the total is occupied by transactions initiated by the Bank of Albania for meeting its operational targets. The section “*settlement for net clearing systems*” contains net settlement transactions resulting from the clearing system, such as: clearing of low value payments in the AECH; clearing of banking and personal cheques in ALL, net settlements of government securities and net settlements of the results of payments in ALL via VISA cards, about which the Bank of Albania plays the settlement agent’s role.

From the viewpoint of surveillance and assessment of payment system stability, the concentration degree of payments at (participating) specific nodes of the network is assessed. The concentration indicators for the AIPS reflect the share of activity of a certain number of banks (3 or 5 banks) to the total activity of this system.

Table 4 Concentration indicators for the AIPS system

	Transaction volume	Value (in ALL billion)
	Share/Total	Share/Total
AIPS system		
3 banks	51%	70%
5 banks	62%	85%
Total (in absolute value)	56,717	5,146

Source: Bank of Albania

Intraday loan facility (ILF) is also an important instrument in the AIPS, which is a collateralized interest-free credit that the Bank of Albania extends to participant banks for managing their intraday liquidity. The procedure for extending an intraday loan is pretty simple and funds are disbursed within 10.00 A.M. of the business day, upon the bank’s request.

Table 5 Number and value of ILFs flowing to AIPS participants

Intraday loan facility	2007	2008
Number of transactions	675	579
Value of transactions (ALL billion)	218	221
Average value of transactions (ALL million)	322	382

Source: Bank of Albania

6.1.2 AUTOMATED ELECTRONIC CLEARING HOUSE SYSTEM - AECH

A total of 113,682 payment transactions were cleared through the AECH system during 2008, with an average value per settled transaction by ALL 150 thousand. Relative to 2007, the cleared payments volume increased 58 percent, while the cleared transactions value increased 47 percent during 2008.

AECH system	2006	2007	2008
Number of transactions	48,889	71,857	113,682
Value of transactions (ALL billion)	7.77	12.01	17.61
Average value per transaction (ALL million)	0.16	0.17	0.15

Source: Bank of Albania

Table 6 Performance of payments in AECH over 2006-2008

The AECH system processes customer payments of below 1 million leks and calculates the net multi-lateral positions for net settlement in the AIPS. Of 16 banks operating in Albania, 14 banks are currently direct participants in the AECH system, processing their customer payments daily in the system. The AECH system processes on average about 462 payments a day, with an average daily value of ALL 71.6 million. The largest volume and value of payments processed in the AECH system is noted during the fourth quarter of 2008.

AECH system	Quarter				Year
	I	II	III	IV	2008
Number of transaction	24,317	29,179	27,872	32,314	113,682
Value of transactions (ALL billion)	3.88	4.45	4.29	5.00	17.61
Average value/transaction (ALL million)	0.16	0.15	0.15	0.15	0.15

Source: Bank of Albania

Table 7 Distribution of payments in the AECH by quarters of 2008

The payments cleared through the AECH system are processed in two sessions (session I - 09.00 to 11.00; and session II - 12.00 to 14.30) during the business day and they are settled for the net result through the AIPS at the end of each session. It is noted that for a one-year period, the largest volume and value of customer payments are cleared in the first session.

AECH system	Section		Year
	I	II	2008
Number of transactions	63,266	50,416	113,682
Value of transactions (ALL billion)	10.69	6.92	17.61
Average value per transaction (ALL million)	0.17	0.14	0.15

Source: Bank of Albania

Table 8 Distribution of payments through the AECH system according to clearing sessions during 2008

The concentration indicators for the AECH system reflect the share occupied by the activity of a certain number of participant banks in the system, against the total activity in this system. The concentration indicator shows that 5 banks own about 63 percent of total low-value payments in the banking system.

Table 9 Concentration indicators for the AECH system

	Volume of transactions	Value of transactions (ALL billion)
AECH system	Share/Total	Share/Total
3 banks	45%	49%
5 banks	63%	64%
Total (absolute value)	113,682	17,612

Source: Bank of Albania

6.1.3 ELECTRONIC PAYMENTS INSTRUMENTS

In view of the publication of statistical indicators on payment instruments in Albania, during 2008 the methodology "On reporting of payment instruments" was reviewed, based on the data the banks report about the payment instruments. The new methodology aims at:

- Collecting and processing the periodical data and establishing a database on the usage of payment instruments in Albania. This is aimed to analyse the tendencies and help the public get acquainted with developments of the payment system in Albania.
- Monitoring the payment system developments, to assess the degree of risks they carry over and ensure transparency in the agreements that have to do with payment instruments and services.
- Complying with the statistics reported by the European Central Bank and the BIS Basle, aiming at providing data on Albania in the Blue Book and Red Book (ECB's publications on payments) in the future.

It results out of banks' reporting that as at end 2008, the total number of bank customer accounts valid for making payments in lek or in foreign currency was 1,573,830, of which about 91 percent are individual accounts. Less than 1 percent of the total number of accounts is accessible through home banking for making payments or for checking the account statement.

Table 10 Total number of bank customer accounts as at December 31, 2008

Account description	Total of accounts	Accessible from home-banking
Customer accounts (1+2)	1,573,830	11,108
1- resident accounts (a+b)	1,564,084	10,751
a - individual	1,429,294	6,958
b - corporate	134,790	3,793
2- non-resident accounts (a+b)	9,746	357
a - individual	9,311	314
b - corporate	435	43

Source: Bank of Albania (Banks' reporting according to the "Methodology on payment instrument reporting").

As at end 2008 there are operating 16 banks in the Republic of Albania, which provide payment services in 438 branches/bank agencies throughout the country. The number of ATMs and POS terminals has risen for card use, respectively by 45 and 61 percent compared to their number at end 2007.

Description	Total
Automated Teller Machines	642
Of which:	
1 - ATMs for cash withdrawal	642
2 – ATMs for transfer orders	59
3 – ATMs for depositing cash	73
Point of Sale terminals	2,953
Of which:	
1- POS terminals for cash withdrawal	907
2- EFTPOS payment terminals	2,915
Terminals for using e-money	-

Source: Bank of Albania (Banks' reporting according to the "Methodology on payment instrument reporting").

Table 11 Number of total ATMs and POSs as at December 31, 2008

A very widespread form of making payments is also the use of electronic payment instruments, which are being used more frequently even in Albania. It is noted that the number of cards circulating increased by 17 percent as at December 31, 2008, compared to 2007. Hence, credit cards issued during this year had a considerable weight. Their number rose by 53 percent relative to 2007.

Number of cards by functions	December 31, 2008
Cards with the cash function	512,232
Cards with the payment function	498,003
Of which:	
1- debit cards	482,072
2- credit cards	15,931
Cards with the e-money function	-
Total number of cards in circulation	512,232
Of which:	
- cards with more than one function	498,003

Source: Bank of Albania (Banks' reporting according to the "Methodology on payment instrument reporting").

Table 12 Total number of banking cards in circulation as at December 31, 2008

The card transactions processed during 2008 is 8,205,143, with a total annual circulation of ALL 93.7 billion. Of total transactions, about 96 percent are cash transactions from ATMs, an indicator of an economy with a large use of cards. In other words, in proportion with the population² in Albania, on average one out of six persons is a card holder. Every card holder performs not more than 16 transactions a year, of which 15 transactions are cash withdrawals from banks. Compared to statistics of the region countries, the Albanian banking system is still in the first steps of using the e-payment instruments.

Transactions through cards by transaction type	Volume	Value (ALL mln)
1- ATMs for cash withdrawal	7,910,609	89,067.43
2- ATMs for depositing	133	2.10
3- Transfer orders through ATMs	271	9.37
4- Cash withdrawals at POS terminals	2,999	451.51
5- Card payments at POS terminals	291,131	4,196.19
Of which:		
- payments through debit cards	187,720	2,013.81
- payments through credit cards	103,411	2,182.38
Total card transactions	8,205,143	93,726.60

Source: Bank of Albania (Banks' reporting according to the "Methodology on payment instrument reporting").

Table 13 Number of total transactions made through banking cards during 2008

As at end 2008 six banks provide home banking service, in the form of products enabling access of the bank account from home, through an internet line or software the bank makes available to the customer.

The use of this service is closely related to the existence of infrastructure and the customer's ability to use internet and up-to-date terminology. Relative to 2007, a higher number and value of home banking transactions were noted in 2008, by 108 and 116 percent respectively.

Table 14 Total number of home banking transactions during 2008

Home Banking	2006	2007	2008
Number of transactions	19,096	42,447	88,261
Value of transactions (ALL billion)	16.83	48.49	104.88

Source: Bank of Albania (Banks' reporting according to the "Methodology on payment instrument reporting")

6.1.4 BANK OF ALBANIA'S ROLE AS SUPERVISOR OF THE PAYMENT SYSTEM

During 2008 it was worked for approaching the existing regulatory framework of the payment system to the *Acquis Communautaire*, and to best international standards of the payment system. In this framework, there were reviewed some regulations and some new regulations were adopted, aiming at their direct adjustment to the EU directives.

i. Regulation "On electronic payment instruments"

The reviewing of this regulation was aimed at improving the regulatory framework for issuing and using the electronic payment instruments, carrying out the Bank of Albania's function for promoting and supervising the smooth functioning of the payment system in the Republic of Albania. The scope of this Regulation is defining the standards of transparency to clients, about conditions, rules and procedures for making payments through electronic payment instruments in the Republic of Albania, determining the type of electronic payment instruments and the way for keeping and reporting information while using them.

ii. Regulation "On the structure and use of international bank account number (IBAN)"

The Regulation "On structure and use of international bank account number (IBAN)", aims at standardising the account numbers used for making payments, with the purpose to promote and improve the payment system in the Republic of Albania. The scope of the Regulation is defining the structure of the international bank account number for use in the Republic of Albania (Albanian IBAN) and specifying the procedures for its creating, checking, validity and use by banks and/or branches of foreign banks licensed by the Bank of Albania.

The project for implementing IBAN in Albania will be carried out in two stages:

- (1) Creating and informing the clients on their account number in the IBAN format. The banks may define on their own only the accurate date of the complete transfer in the IBAN format, as well as the transfer process duration, provided the transfer is completed within June 1, 2009.
- (2) The compulsory use and checking of the IBAN for all the sent/received payments to/from banks. Starting from January 1, 2010, banks are obliged to check the validity of IBAN of the sender/beneficiary's account included in the payment instruction, incoming and outgoing money transfers, irrespective of the information received on the IBAN via e-mail or a letter. Starting from that date, the Albanian payment systems will check the validity of accounts included in the payment instructions and will reject oral payment orders, in case of inaccuracy.

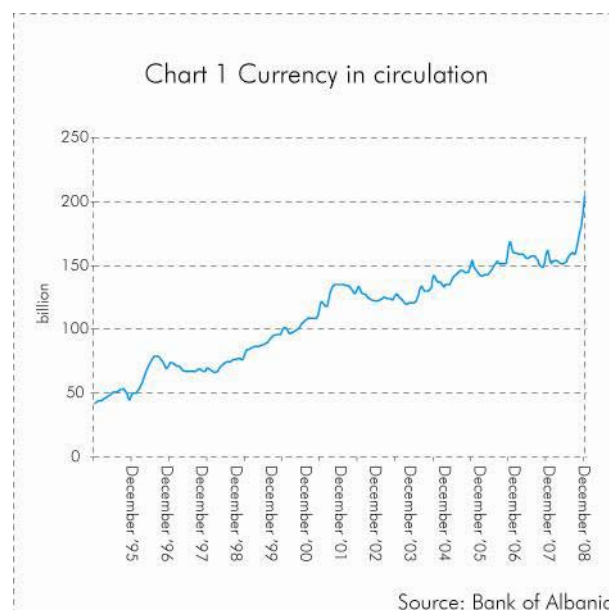
iii. Document "Policy of supervising payment and settlement systems"

The document "Policy of supervising payment and settlement systems" aims to clarify the supervision targets on payment and settlement systems, the Bank of Albania's role, the area where supervision is applied, the way the supervision process is carried out, principles and standards where this process is based on, as well as the cooperation with other supervisory authorities. The document specifies essential responsibilities of the central bank in supervising the payment system and in carrying out these responsibilities, the objectives and activities of supervision based on international principles and standards. It also underlines the need for cooperating with other central banks and supervisory institutions.

To further fulfil the legal framework of a modern payment system, it is assessed as urgent the need for drafting an Albanian law "On the payment system", whose compilation has already started. The commitment of the state institutions and the cooperation with commercial banks will help the Bank of Albania to accomplish this goal, as a necessary condition for the operation of the national payment system and compliance with the EU directives.

6.2 MONEY ISSUE

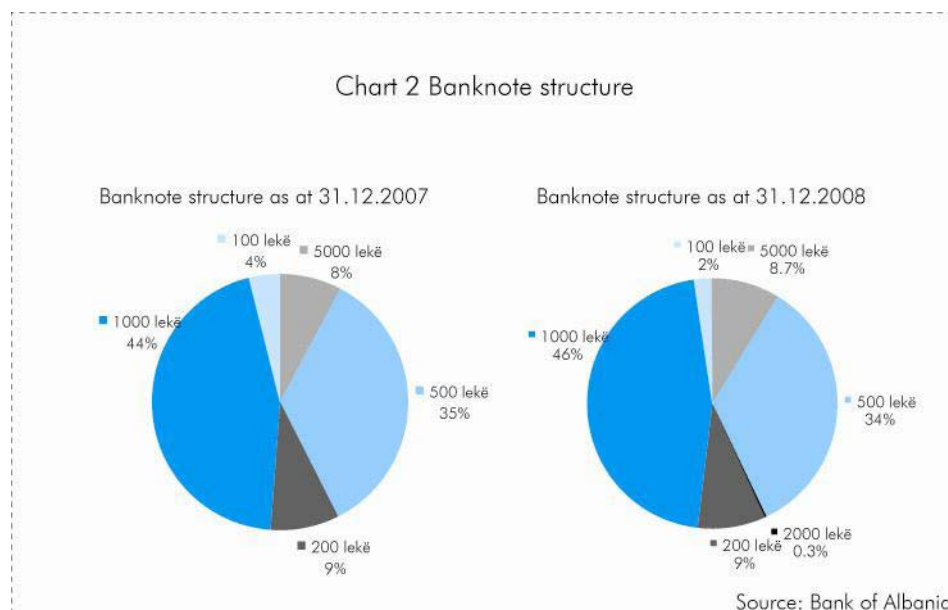
Currency in circulation at the end of 2008 amounted to ALL 203,713,429 thousand, compared to ALL 161,161,883 thousand at end 2007. The largest growth was noted in the fourth quarter, a period corresponding to the unexpected developments in the international financial market and their resonance even in the domestic market.



6.2.1 STRUCTURE OF CURRENCY IN CIRCULATION

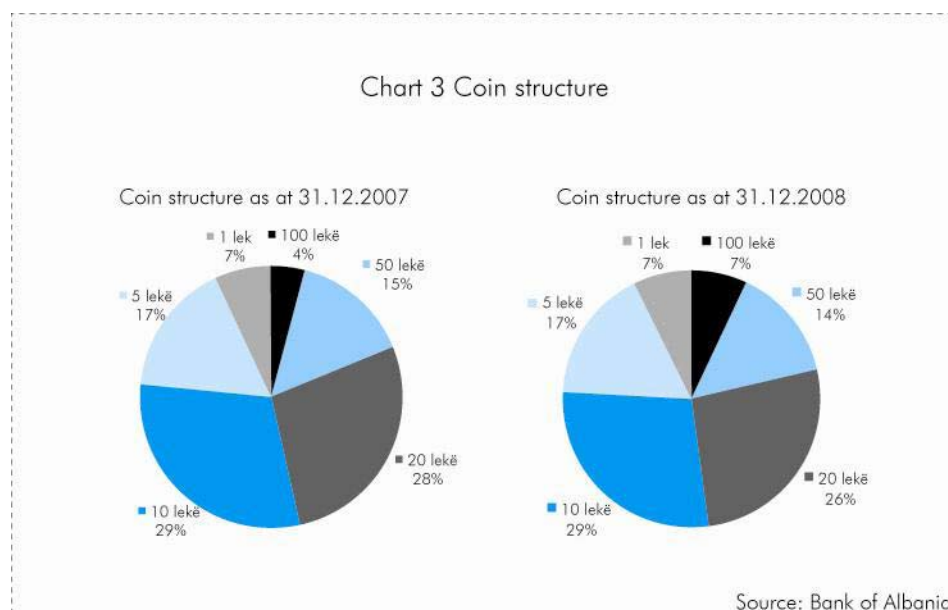
BANKNOTE

The structure of banknote in circulation was characterised by a rise in the share of high (1000 and 5000 Lek) denominations, mainly dictated by the demand of second tier banks, facing the flow of increasing payments and filling the ATMs with the above-mentioned denominations. At end of December 2008 the new banknote of 2000 lek denomination, legal tender, was put into circulation for the first time.



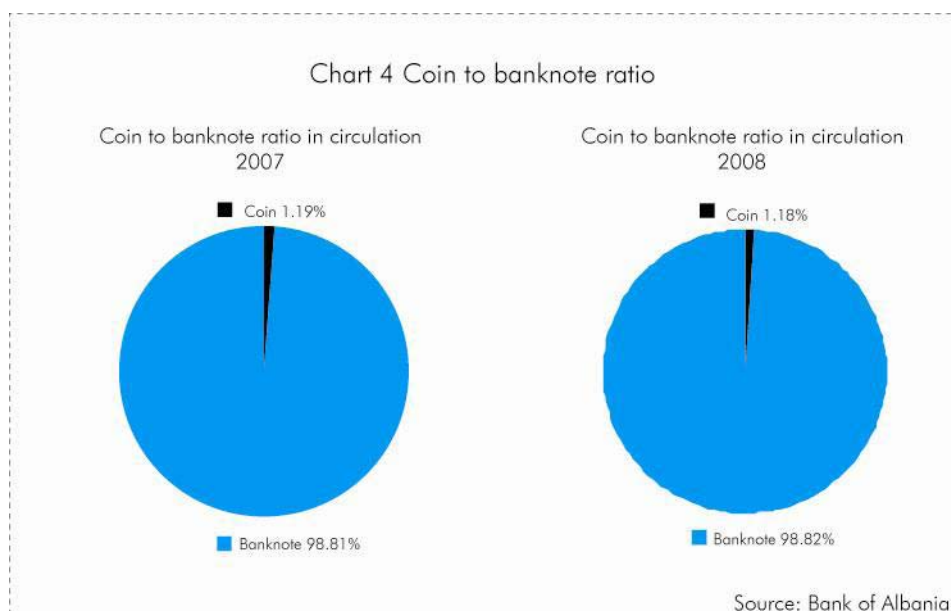
COIN

The coin structure even for 2008 continued to be oriented towards a rise in the share of large (50 and 100 Lek) denominations. One of the main factors impacting on this rise was the use of those coins to substitute the 100 Lek note, which ceased to be legal tender on 31 December, 2008.



- *COIN VERSUS BANKNOTE*

At end 2008 the overall value of banknote to coin ratio resulted almost equal to that of the previous year. The gradual replacing of 100 Lek note with the coin and the demand for coins from retail traders and mainly from new supermarkets were the main factors explaining why the ratio remained unchanged, notwithstanding the obvious banknote growth.



6.2.2 CURRENCY IN CIRCULATION INDICATORS

THE AVERAGE VALUE OF BANKNOTE IN CIRCULATION

The average value of a banknote in circulation at end 2008 is estimated at 1,065 lek, from 1,013 lek it was at the end of 2007.

MONEY RETURN COEFFICIENT

The coefficient of money return to the Bank of Albania as at end 2008 was 0.575, compared to 0.750 in 2007. This indicates that in relation to currency in circulation, second tier banks returned less money to Bank of Albania's cash register during 2008, which is also reflected in the growth of money in circulation.

QUALITY OF CURRENCY IN CIRCULATION

Pursuant to contemporary standards and rapid increase of the number of ATMs at second-tier banks, even during 2008, the Bank of Albania withdrew from circulation about 19.4 million useless banknotes, replacing them with useful banknotes. About 40 percent of the quantity withdrawn is composed by issues of earlier than 1996. The new banknotes put into circulation in 2008 account for 27.74 percent of the total average of banknotes in circulation.

BANKNOTE PRINTING AND REPRINTING

During 2008 there was printed for the first time and put into circulation the new 2000 Lek note, legal tender. Its putting into circulation prevented the gap existing between 1000 Lek and 5000 Lek denominations, facilitating the performance of cash operations by the public. Also, during 2008 the 1000 Lek denomination, issue of 2007, was reprinted and put into circulation.

NOTES WITHDRAWN FROM CIRCULATION

On 31 December, 2008, the 200 Lek note, issue of 1993, 1994, 1996 and the 100 Lek note, issue of all years, ceased to be legal tender.

6.3 PUBLIC RELATIONS

A special importance in the daily activity of the Bank of Albania is attached to communication and public relations, since an open and transparent communication helps raising the credibility and effectiveness of its decision-making. Besides legal obligations and official communication, during 2008 the Bank of Albania attempted to carry out an interactive and direct communication with various groups of the Albanian public.

During 2008, the Governor of the Bank of Albania carried out several activities and meetings with financial and banking system actors, with different representatives of media and academics, held lectures at high schools and universities, peaking with the organisation of a regional meeting in Kukës, which gathered around a discussion table representatives of the banking system, local government and academics of Albania and Kosovo.

The official communication of the Bank of Albania was based on the following institutional pillars:

1. Public presentations of the Governor: speeches, interviews, press statements, transmitting to the public the Bank of Albania's stance on certain current issues.
2. Periodical publications of the Bank of Albania: The Bank of Albania publishes a complete set of reports on its important activities, such as on monetary policy, banking supervision, financial stability, payment systems, etc. Through them, it conveys to the public not only the results achieved through its work but also the decision-making process and its utility in fostering the Albanian economy.
3. Bank of Albania's web-site continues to be regarded by us as an efficient tool for informing the public about our role and work in a real time. It is visited by an ever increasing number of interested persons.
4. The Governor's award for the Best Diploma, a competition opened throughout Albania for the newly-graduate students, which aims to promote the scientific research in issues related to the Albanian economy and its banking system, thus impacting on increasing research capacities in this area.

5. The economic-financial education of the public, an initiative of the Bank of Albania to develop the economic culture of the Albanian society, with the purpose to create an environment that takes rational economic decisions and operates in accordance with the central bank signals.

The economic and financial education of the public is already transformed into an institutional philosophy, which is reflected in concrete actions. In this framework, the Bank of Albania has designed comprehensive education programs, intended to be applied with different groups of interest.

During 2008 our educational program "Central Bank in Everyday Life" was extended even in Vlora, besides Tirana. Training workshops took place in both districts, with high school teachers of economics; educational brochures were distributed at schools; meetings and discussions about the central bank and its role in the economy were conducted with teachers and pupils; educational questionnaires were distributed in order to obtain their opinion about the educational work of the Bank and about their knowledge on the central bank; the board "Central Bank in Everyday life" was set up and will be gifted to schools to be placed at their halls; A competition titled "The Real Value of Money" was carried out with high-school pupils, for their knowledge on the central bank. All these educational activities carried out by the Bank of Albania with pupils and teachers were aimed at understanding and raising the understanding of this group of interest about the role, objectives and functions of the Bank of Albania. For reasons related to teacher's profession, but also to the role of the new generation in the country's future, the group of pupils and teachers was treated with special attention by the Bank. Teachers, through their everyday work transmit knowledge to their pupils, but also to the environment they live in. On the other hand, the young people will soon enough be active participants in the country's economic life and as such, with their decisions they are going to play an important role in it.

During 2008 the educational program was based on three main directions:

- *EXPANSION OF THE NUMBER OF GROUPS OF INTEREST INCLUDED IN THE EDUCATION PROGRAM "CENTRAL BANK IN EVERYDAY LIFE"*

During 2008 the Bank of Albania has worked for the public education, not only by extending its education program to already-included groups, but also by expanding it and incorporating other groups of interest in it. Given the principle that we are assisted in accomplishment of our objectives, placed in a well-educated environment about finances, during 2008 the Bank established a cooperating relations even with representatives of non-profit organisations and institutions interested in the field of education. The Governor of the Bank of Albania met representatives of this group and exchanged ideas about this joint commitment, under the slogan "There is always something new to learn about money!" Our target is to make this group of interest act as an intermediary, so that we arrive at the broad public.

Our educational program has included social workers as well. Given the features of their profession, their direct contacts with the so-called “general public”, the social workers are regarded by the Bank as its “ambassadors”.

A specific training program was designed and carried out with this group of interest, aiming at creating knowledge about the Bank of Albania’s activity and its role in the country’s economy in general and in the everyday life in particular.

Finally, almost all participants of this training program were enrolled in the list of distribution of the Bank’s publications and keep constant contacts with it.

- *STUDENTS’ GROUP*

In 2008 the Bank of Albania continued to keep a constant relationship with students of different universities of the country, particularly with those of economics branch.

The Governor of the Bank of Albania, in different periods of the year and according to a certain schedule, delivered lectures on various topics at university auditoriums. These lectures were associated with organising the “Bank’s Day” for students. The activity was set up on a standard format, for all faculties. A mini-fair with Bank’s publications was set up at their premises, and free discussions were conducted with groups of students.

Also, in those universities, the Bank’s formal publications (periodical reports), different scientific articles published in those publications, working papers and brief versions of scientific researches held in activities organised by the Bank, educational brochures and leaflets continued to be distributed at a considerable number. The university libraries of the country are enrolled in the Bank’s official list for the distribution of publications and benefit from them regularly.

Our Bank’s library is open to students once a week, but it also helps them during other days as well, upon their request and pursuant to the Bank’s regulation.

- *BANK OF ALBANIA’S PUBLICATION BOARDS*

During 2008 there were lodged educational publication boards of the Bank at the premises visited by customers of commercial banks that conduct their business in Tirana. Bank customers have received a great number of brochures and leaflets. Such boards are also lodged at the premises of large trade centres in Tirana, during certain periods of time. It turned out to be a good way, so as the public gets acquainted with and makes use of many educational publications the Bank Albania prepares for the public.

Year 2008 also recorded the largest territorial expansion of the educational work. Hence, besides Tirana, other districts, such as that of Vlora, Kukës, and later on Korça, Gjirokastra and Shkodra were also incorporated.

6.4 EUROPEAN INTEGRATION AND INTERNATIONAL COOPERATION

6.4.1 EUROPEAN INTEGRATION ISSUE

Further to the signing of the Stabilization and Association Agreement (SAA) with the EU Member States on June 12, 2006, during 2008, the ratification process of this agreement continued with the Member States. Until the end of 2008, the SAA was ratified from 24 Member States of the EU, while it is expected to enter into force in 2009. At the same time, during this year, there continued the implementation of the Interim Agreement on Trade-Related Issues between Republic of Albania and the European Union, which entered into force on 1 December, 2006.

The obligations stemming from the SAA on the Bank of Albania are related with the meeting of the economic Copenhagen criteria for EU membership, guaranteeing the right of decision-making and the freedom to provide financial services to European community banks and other financial institutions, liberalization of capital flows and payments between Albania and the EU; and approximating the Albanian legislation with the European (*acquis communautaire*) in these areas.

During 2008 the Bank of Albania has kept regular contacts with the Ministry of European Integration and has posted there its monthly progress reports, which reflect the progress achieved in terms of implementing the legal measures and applicable activities, in line with the terms specified under the National Plan for the Implementation of the SAA as well as a description of the degree of compliance of legal acts adopted by the Bank of Albania with the *acquis*.

In the framework of the National Plan for the Implementation of the SAA (2007-2012), the Bank of Albania went on working for its legal incentives and applicable activities. Hence, pursuant to the Law "On Banks in the Republic of Albania", which entered into force in June 2007, the regulatory framework of banking supervision, particularly in terms of management, transparency and internal audit of banks was reviewed.

On 5 November 2008 the European Commission published the 2008 Progress Report on Albania, associated with the 2008-2009 Development Strategy of the European Union. Both these documents described the progress made by Albania and the challenges it is faced with, designing simultaneously even the approach of the European Commission to guide and support our country in the future. The report highlighted the progress achieved by Albania over the period 1 October 2007 - 30 September 2008 in terms of meeting the Copenhagen criteria.

The European Commission's report highlighted the ongoing political consensus on essential economic policies and the maintaining of macroeconomic stability in the country, while it commended the rapid paces

of the economy and the credibility of Bank of Albania's monetary policy on keeping inflation within the set target.

At the same time, the European Commission underlined the financial system stability, which was supported by a favourable economic environment and strengthening of financial supervision. Also, the report commended the positive developments in the country's banking system, laying emphasis on the strengthening of prudential banking supervision with the aim to maintain the loan portfolio quality and assess the regulatory framework of banking supervision in terms of constant approximation to best international standards.

The Commission appraised the approval of a number of regulations in implementation of the new Law "On Banks in the Republic of Albania", which omitted the provisions that related to differentiated treatment branches of foreign banks and the Albanian banks, while it also commended the payment system projects. It also made an appeal for further strengthening of prudential banking supervision and for enhancing the cooperation among regional supervision authorities.

The Commission accentuated in the report the need for making changes to the legal framework related to liberalization of free capital mobility, in accordance with the obligations stemming from the SAA.

The Bank of Albania took part regularly in the periodic meetings conducted between the Republic of Albania and the EU during 2008, such as the Meeting on the Domestic Market and Competition and the Meeting on Economic-Financial Issues and Statistics, where the Bank of Albania presented the main developments in monetary policy area, exchange rate, external sector and the banking system. At the same time, the Bank of Albania was also represented in the XII Meeting of the Joint EU-Albania Commission, conducted on December, where recent economic developments of the country were reported.

On 19 December 2008 the European Commission established the IPA National Program for Albania under the transition assistance and institution building component for 2008. The instrument of pre-accession assistance (IPA) constitutes the financial assistance of the EU.

Also, part of the Albanian projects that will be financed from IPA 2008 is also the twinning project of the Bank of Albania with two or three member central banks of the European System of Central Banks, aiming to strengthen its institutional capacities, particularly the banking supervision area, statistics, payment system and monetary policy implementation. The main goal of this project was to prepare the Bank of Albania towards the European integration, thus helping to approximate and harmonise the regulatory and legal framework, and to improve the current practices according to standards of the European System of Central Banks.

The project is aimed at contributing to the meeting of the economic Copenhagen criteria, through efficient implementation of monetary policy

and establishment of a secure, stable and well-developed banking system. The project is drafted in accordance with the priorities reflected in the strategic documents between the EU and the Republic of Albania, such as the European Partnership Document for Albania, the Multi-Annual Indicative Planning Document (MIPD) 2007-2009, and the National Plan for the Development of the SAA 2007-2012.

For the first time during 2008 the Bank of Albania benefited technical assistance from the TAIEX instrument (*Technical Assistance and Information Exchange*) of the European Union. This instrument provides technical assistance for approximation with and implementation of the European Community legislation of the candidate countries and potential candidate countries, through visits of European experts to the country, organisation of various seminars and workshops, as well as through the organisation of study visits to the institutions of the EU countries.

So, further to applications made by the Bank of Albania at end of 2007 to the TAIEX unit of the European Commission, during 2008 there was organised a work visit of a Slovenian expert on the amendments to the Law "On the Bank of Albania" and a seminar on free capital mobility, with the participation of Bank of Albania's staff, AMF, Ministry of Finance, Ministry of Economy, Trade and Energy and Bank's Association.

6.4.2 INTERNATIONAL COOPERATION

- *RELATIONS WITH THE INTERNATIONAL MONETARY FUND (IMF)*

The Republic of Albania joined the International Monetary Fund on October 1991. Its quota during 2008 remained unchanged, at SDR 48.7 million³, as did its votes (737 votes or 0.03% of the total votes of all IMF members). Albania is at the same constituency as Italy, Greece, Portugal, Malta, San Marino and East Timor. This constituency is entitled to a total of 90.968 votes (or about 4.1 percent of total votes of all IMF members) and is led by the Italian representative, Mr. Arrigo Sadun, who acts as Executive Director of the constituency.

On 14 March and 11 July 2008 the Albanian authorities represented by the Prime Minister, the Governor of the Bank of Albania and the Minister of Finance officially submitted to the IMF the Memorandum of Understanding and the Memorandum of Economic and Financial Policies.

Based on such documents and assessments from IMF review missions that visited Albania in October-November 2007 and April-May 2008, the IMF Executive Board carried out the fourth and the fifth review, respectively on March 28 and July 25, on Albania's progress as per the implementation of the three-year PRGF/EFF agreement, approved on January 27, 2006. These reviews made possible the disbursement of the sum total of SDR 4.8 million for Albania during 2008, driving the total amount extended since the agreement signing to SDR 14.6 million.

The Executive Board conferred its conclusions at the end of these reviews that the macroeconomic performance of Albania is robust, the economic growth is optimistic and the existing monetary policy framework is appropriate, thus reflecting the strong commitment of Albanian authorities in pursuing right macroeconomic policies.

During 2008 Albania was visited by the fifth and sixth IMF review missions. The visit of the fifth review mission of April-May, besides consultations on assessing the implementation of obligations stemming from the three-year PRGF/EFF agreement, was also focused on consultations about Article IV of "Articles of IMF Agreement", whereas the sixth (the last) review mission of October-November was focused mainly on assessing the implementation of tasks deriving from the three-year PRGF/EFF agreement.

Moreover, Albania has paid about SDR 10.1 million to the IMF in 2008, in the framework of paying off its dues (principal payments, interests, periodic expenditures, etc), inherited from the past PRGF agreements and the existing PRGF/EFF one.

At the same time, the Governor of the Bank of Albania has regularly represented the Republic of Albania in the decision-making process of the Board of Governors, which is the highest body of the IMF. Of importance in the relations with the IMF during 2008 were the spring and annual meetings of the IMF and the World Bank, held in April and October respectively. During these meetings the bank of Albania delegation, headed by the Governor met with senior representatives of the IMF, to discuss recent macroeconomic developments and matters that pertain to the monetary and financial stability. In the process, very good relations between the IMF and Albanian authorities have been established, while it has been commended the good work of the Bank of Albania in keeping inflation under control and in strengthening credibility and public confidence. Senior IMF representatives have expressed their willingness to continue the technical assistance projects for the Bank of Albania.

During 2008 the Bank of Albania was visited also by an advisory mission for the drafting of 2009 budget. The Bank of Albania continued to benefit from IMF technical assistance relative to its staff training even during 2008. The IMF gave advice on improvement of the monetary policy drafting process, models and economic forecasting, further development of banking supervision capacities, etc.

- *RELATIONS WITH THE WORLD BANK GROUP*

Albania is a member of the World Bank Group since 1991 and has benefited from this institution a total of Eur 997.5 million funds for 67 projects. During 2008, based on high achievements of economic growth, Albania gained the status of an average-income country, a very positive signal for investors and foreign financial markets for the economic future of the country.

Even during 2008 this cooperation of the Bank of Albania with the World Bank Group continued in the framework of the agreement "On management and advice of foreign reserve investment" signed in September 2005. So, the World Bank Group provided technical assistance to the Bank of Albania through the RAMP (Reserve advisory management program), in the framework of Sovran Partnership Investments (SPI). This advice and technical assistance was made concrete through visits of experts of World Bank Treasury and the participation of Bank of Albania's employees in seminars organised by the World Bank abroad. The technical cooperation in the framework of the RAMP program is focused on the drafting of a new regulatory basis and addressing some technical issues related to foreign reserve management.

In January-February, with the support of the Convergence Program of the World Bank, a discussion meeting took place in Tirana, organised in two sets, titled: "On approximation with the EU for a better regulatory framework", with the purpose to familiarise the Bank of Albania's staff with some applications of legal and economic issues in terms of drafting the regulatory policies, organising the regulatory processes according to practices that prevail on the EU, getting acquainted with the analytical techniques in drafting its regulatory policies, etc.

In meetings organised by the Bank of Albania's delegation with top representatives of the World Bank Group in the framework of spring and annual meetings of the IMF and the World Bank, the economic developments of Albania and the measures taken by the Bank of Albania in terms of maintaining macroeconomic stability and inflationary pressures were presented. The representatives of the World Bank, in turn, have expressed their support to steps made by the Bank of Albania and have rendered their assistance in relation to the improvement of financial infrastructure, laying special emphasis on the development of microfinance institutions and savings and loan associations.

- *RELATIONS WITH OTHER INTERNATIONAL FINANCIAL INSTITUTIONS*

During 2008 the Bank of Albania continued to keep contacts with the European Bank for Reconstruction and Development (EBRD), mainly in terms of providing information and statistics on the deployments of the Albanian economy in general and the financial sector in particular. In the 2007 Transition Report, The EBRD has positively assessed the monetary policy stance of the Bank of Albania in terms of keeping inflation within the targeted band and the strengthening of banking supervision through the new Law "On Banks in the Republic of Albania" which entered into force in June 2007, as well as the taking of measures on banks with a high rate of non-performing loans or with a high rate of lending growth.

In the framework of encouraging the cooperation between Albania and the EBRD, an official visit took place at the Bank of Albania of a Polish delegation, composed of the President of the National Bank of Poland and the Representative Directorate of the Group Albania – Bulgaria – Poland

and EBRD, which expressed the EBRD's commitment to continue the financial support and investments in Albania, in accordance with the priority areas specified in the strategy of this institution.

At the same time, the Bank of Albania continued keeping close relations with the Bank for International Settlements (BIS) during 2008. The Governor of the Bank of Albania took part in the 78-th Annual Meeting of the BIS, held in June in Basle, Switzerland, emphasising in the meetings held with representatives of this institution and other member banks, the importance of expanding the technical cooperation between the Bank of Albania and other central banks in joint-interest areas. The BIS has been especially active in rendering the technical assistance to the Bank of Albania through workshops and seminars organised by the Financial Stability Institute, which promoted the international financial stability through exchange of information and cooperation in financial system's supervision.

- *RELATIONS WITH CENTRAL BANKS AND THE TECHNICAL COOPERATION*

Further to the intensification of bilateral relations with other central banks, the Governor of the Bank of Albania carried out during 2008 an official visit to the Bank of Israel, National Bank of Sweden and Bank of Canada, meeting his homologues, while he has also taken part in many regional and international seminars and conferences. These visits and conferences have helped further consolidation and development of the ever-increasing technical cooperation between the Bank of Albania and these institutions.

For the first time during 2008, the Governor Fullani represented the Bank of Albania in the fifth Euro-Mediterranean seminar, an annual high-level forum, which brought together representatives of the Eurosystem and Mediterranean central banks, non-members of the Euro-zone. The seminar was focused on recent economic and financial developments of the Mediterranean countries, monetary policy strategies and exchange rate regimes, as well as developments in the banking sectors and implications for financial stability.

In the regional plan, it's worth mentioning the XIX Governors' Club Meeting of the Black Sea, Central Asia and Balkan, hosted by the Bank of Albania in May, where among guest of honour was the Vice President of the European Central Bank, Mr. Lucas Papademos. In the meantime, the Bank of Albania participated in the XXth Club meeting held in Sarajevo on September. During 2008 the Bank of Albania served as the vice chairman of this Club.

Also in the regional plan, following the Bank of Greece initiative the Governors and heads of the supervisory authorities of the region held two meetings, in Athens and Sofia. The meetings were carried out in the framework of the joint memorandum of understanding, signed in Athens on July 2007, which aimed at further enhancing the cooperation in banking supervision area in South East Europe, as well as maintaining the financial stability in the region. The memorandum defines the areas and terms of cooperation through

banking supervision authorities, in compliance with the existing supervisory and regulatory regimes in each country.

In May a delegation of the Central Bank of the Republic of Kosovo, headed by the Governor Mr. Hashim Rexhepi, carried out an official visit to the Bank of Albania, commending not only the excellent cooperation relations between both institutions, but also expressing the willingness for continuing this technical cooperation.

During 2008 the Bank of Italy, the National Bank of Austria, the National Bank of Czech Republic, the National Bank of Poland and the National Bank of Sweden have been the largest providers of the technical assistance to the Bank of Albania, mainly by organising workshops and seminars, as well as work visits of foreign experts to the Bank of Albania. At the same time, there are intensified technical cooperation relations with central banks of Bulgaria and Rumania, as countries acceded recently to the European System of Central Banks. Continuation of long-term technical cooperation with the National Bank of Sweden in the areas of drafting and implementing the monetary policy, monetary operations and financial stability constitutes another important highlight for 2008.

In 2008, likewise in the past, in view of cooperation and technical assistance, the provision of technical assistance by the Bank of Albania to the Central Bank of the Republic of Kosovo focused on areas such as internal audit, information technology and payment system, off-site supervision, human resources, legal service, etc.

6.5 AMENDMENTS TO BANKING LEGISLATION

The Bank of Albania, being the responsible authority for the implementation of the Law No. 9662, dated 18.12.2006 "On Banks in the Republic of Albania", undertook the initiative of drafting and approval of the Law No. 9974, dated 28.07.2008 "On entitlement repurchase agreement".

Upon entry into force of this law, the efforts of the Bank of Albania were finalized for establishing a proper legal infrastructure for the development of repurchase agreements market among commercial banks, contributing not only to enhancing the monetary policy transmission efficiency, but also creating the possibility for using these agreements as a flexible instrument, in order to ensure and invest liquidity in the interbank market.

Another important legal amendment was the approval of some changes to the Civil Code Procedure in the Republic of Albania, having to do mainly with easing and shortening of the time frames of procedures for credit collateral execution.

Pursuant to and for the implementation of the Law No. 8269, dated 23.12.1997 "On the Bank of Albania", amended, the Bank of Albania

drafted, in the framework of cooperation with the Deposit Insurance Agency, the draft law "On some amendments and changes to the Law No. 8873, dated 29.03.2002 "On Deposit Insurance". This draft law aims mainly at approximating the legal framework related to the compensation scheme of insured deposits and the defining of competencies of the Agency, in view of the steps of our country's integration to the European Union and improvement of legal conditions for the smooth functioning of the banking system in the Republic of Albania.

- *IMPROVEMENT OF THE LEGAL AND REGULATORY FRAMEWORK RELATED TO PAYMENTS AND PAYMENT SYSTEMS*

One of the secondary objectives of the Bank of Albania is "promoting and supporting the payment systems", and in view of meeting this objective, its primary task is "promoting the smooth functioning of the payment system".

To this end, the Bank of Albania over the second half of 2008, in cooperation with the International Monetary Fund started the work for compiling the draft law On the Payment System in the Republic of Albania, which is under discussion with interested stakeholders. The approval of this law is an obligation deriving from the SAA and the European Partnership Document, as well as from medium-term priorities required under the National Plan for the Implementation of the SAA.

In recent years the promoting and supporting of the payment system development is assuming great importance, being defined in central banks' statutes as their secondary objective important to them, along with the financial stability. This is so for the fact that a non-efficient payment system impedes the financial stability of the country (obstacles in making transfer; liquidity shortages; banks' insolvency; financial system destabilization), what might bring about also the impediment of price stability, which is a central bank's primary target.

Also, in the framework of measures for curtailing cash in the Albanian economy, the Bank of Albania has undertaken some regulatory measures, aiming at upgrading the payment system and payments in the Republic of Albania.

- *POLICY OF SUPERVISING PAYMENT AND SETTLEMENT SYSTEMS*

The Bank of Albania, through the decision No. 38, dated 11.06.2008 of the Supervisory Council approved the document "Policy of supervising payment and settlement systems", through which the Bank of Albania's role is specified relative to payment system supervision; payment system supervision targets; supervision principles and standards on payments and settlement systems; entities subject to Bank of Albania's supervision; activities that the Bank of Albania carries out for meeting the objectives; and the cooperation with the entire banking supervision.

- *ELECTRONIC PAYMENT INSTRUMENTS*

The Bank of Albania, through its decision No. 11, dated 06.02.2008 of the Supervisory Council, approved the Regulation "On electronic payment instruments" whose scope is the specification of standards of transparency to customers concerning conditions, rules and procedures of making payments through e-payment instrument in the Republic of Albania; types of e-payment instruments, as well as the manner to protect and report information while using e-payment instruments.

The Regulation was aimed to adopt best standards on issuing and using e-payment instruments pursuant to the EU directives and recommendations and best central bank practices.

- *IMPROVEMENT OF THE LEGAL FRAMEWORK ON FINANCIAL ACTIVITY SUPERVISION*

During 2008, the Bank of Albania, after ascertaining legal ambiguity in the implementation of the Law No. 9396, dated 12.5.2005 "On Financial Leasing", amended, and the Law No. 9630, dated 30.10.2006 "On the Factoring" amended, in terms of regulating the supervision-related issues of financial leasing and factoring activity by entities required under both laws, proposed relevant alterations, which have already entered into force after being passed by the Albanian Parliament.

The amendments made to both laws aim to improve the legal framework concerning the inclusion of trade entities whose only scope is to carry out the financial leasing activity or the factoring one, under the supervisory authority of the Bank of Albania, thus preventing any legal situation that might pose risk to the financial stability in the future and any possibility of abuse for illegal purposes by those companies.

- *ALTERATION OF THE LEGAL FRAMEWORK UPON ENTRY INTO FORCE OF THE LAW "ON BANKS IN THE REPUBLIC OF ALBANIA"*

During 2008, the Bank of Albania continued the process of reviewing the existing regulations in supervision area, with the purpose to adjust them to the requirements of the new Law "On Banks in the Republic of Albania", which entered into force on 01.06.2007, as well as to further approximate legislation to the *Acquis Communautaire* in this area, in accordance with the commitments stemming from the SAA.

The Bank of Albania approved the Regulation "On internal audit system at banks and branches of foreign banks". The Regulation puts in focus the internal audit process and system in banks and branches of foreign banks, as an important part of the overall governance of banks. It provides the requirements and rules for organising the internal audit applicable by entities subject to this Regulation. It contains some basic criteria that aim to promote a sufficient internal audit system, as a key factor in banks' management and governance.

The Supervisory Council approved the Regulations “On transparency about financial and banking products and services” and “On minimum requirements of publication of information from banks and branches of foreign banks”. Both regulations harmonise the new requirements of the Law “On Banks in the Republic of Albania” related to *banks’ transparency on all products and services* supplied to customers and the broad public and the strengthening of the market discipline, in terms of increasing the requirements for publication of information on the financial position and risk profile of banks and branches of foreign banks, etc..

The Regulation “On minimum requirements for publication of information by banks and branches of foreign banks” was drafted on the basis and in implementation of the requirements of the Law “On Banks in the Republic of Albania” and the requirements of the third pillar – Market discipline, of the New Capital Accord (Basle II) of the Basle Committee. It stipulates the core regulatory requirements of the supervisory authority for the publication of information from banks and branches of foreign banks to the public and market participants.

Also, there were approved some amendments to the Regulations “On credit risk management”; “On capital adequacy ratio” and “On operational risk management at branches of foreign banks”. These changes relate to credit risk management and are an ongoing strengthening of measures taken by the supervisory authority for minimising the credit risk from banks of the system. The regulations provide chiefly the special measures for monitoring the risk from lending in foreign currency or indexed with the exchange rate, which may pose risk, mainly in cases when borrowers generate their income in the domestic currency.

Approval of the Regulation “On minimum technical and security conditions of work premises at the entities licensed by the Bank of Albania”, stipulates in details the technical and security conditions around bank windows and related to management of monetary values, the requirement on security staff for premises and the requirement for the transportation and accompanying of the physical monetary values, based on the Law “On safeguarding and physical security service”. It has also provided several new additional requirements about technical conditions and security of foreign exchange bureaus and non-bank financial entities.

ENDNOTES

¹ GDP rate, obtained from "IMF Country Report – February 2009"

² INSTAT – Population number, January 2008

³ On 31 December 2008 (referring to the official website of the IMF), the exchange rate of SDR with the American dollar and the euro was: 1 sdr = 1.540270 usd, 1 sdr = 1.106750 euro.

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CHAPTER VII INDEPENDENT AUDITORS' REPORT AND FINANCIAL STATEMENTS AS OF AND FOR THE YEAR ENDED DECEMBER 31, 2008



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INDEPENDENT AUDITORS' REPORT

To the Supervisory Council of Bank of Albania
 Tirana, 11 March 2009

We have audited the accompanying financial statements of Bank of Albania ("the Bank"), which comprise the balance sheet as at 31 December 2008, and the income statement, statement of changes in equity and cash flow statement for the year then ended, and a summary of significant accounting policies and other explanatory notes. The corresponding figures presented are based on financial statements of the Bank as at and for the year ended 31 December 2007, which were audited by another auditor whose report dated 7 March 2008 expressed an unqualified opinion on those statements.

MANAGEMENT'S RESPONSIBILITY FOR THE FINANCIAL STATEMENTS

Management is responsible for the preparation and fair presentation of these financial statements in accordance with the accounting policies adopted by the Supervisory Council of the Bank of Albania as disclosed in Note 2 (a) to the financial statements. This responsibility includes: designing, implementing and maintaining internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatements, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances.

AUDITORS' RESPONSIBILITY

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing. Those standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance whether the financial statements are free of material misstatement.

KPMG Albania Sh.p.k., an Albanian limited liability company and a member firm of the KPMG network of independent member firms affiliated with KPMG International, a Swiss cooperative.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting principles used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

OPINION

In our opinion, the financial statements give a true and fair view' of the financial position of the Bank as at 31 December 2008, and of its financial performance and its cash flows for the year then ended in accordance with the accounting policies adopted by the Supervisory Council of the Bank of Albania as disclosed in Note 2 (a) to the financial statements.

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FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2008 (WITH INDEPENDENT AUDITOR'S REPORT THEREON)

BALANCE SHEET AS AT 31 DECEMBER 2008 (AMOUNTS IN LEK MILLION, UNLESS OTHERWISE STATED)

	Notes	31 December 2008	31 December 2007
ASSETS			
Assets denominated in foreign currencies			
Gold and precious metals	5	5,265	923
Deposits with the International Monetary Fund	6	6,910	7,031
Deposits with non resident banks	7	58,824	40,976
Available for sale investments	8.1	132,339	124,096
Held for trading investments	8.2	10,614	8,747
Other foreign assets	9	1,577	752
Total assets denominated in foreign currencies		215,529	182,525
Domestic assets			
Gold and precious metals	5	2,462	63
Transit credits	10.1	69	95
Loan to Albanian Government	10.2	3,000	-
Loans to resident banks	10.3	20,072	1,509
Available for sale investments	11	74,594	66,523
Investments in local currency	12	-	5,909
Other domestic assets	13	4,547	3,503
Total domestic assets		104,744	77,602
Total Assets		320,273	260,127
LIABILITIES			
Liabilities denominated in foreign currencies			
Due to the International Monetary Fund	14	12,869	13,946
Due to non-resident financial institutions	15	1,178	1,183
Other foreign liabilities		261	251
Total liabilities denominated in foreign currencies		14,308	15,380
Domestic liabilities			
Currency in circulation	16	203,713	161,162
Due to resident banks	17	67,803	67,051
Due to the Government	18	21,096	14,313
Deferred income		-	3
Other domestic liabilities	19	1,480	927
Total domestic liabilities		294,092	243,456
CAPITAL AND RESERVES			
Capital	20	2,500	2,500
Legal reserve	21	7,515	5,181
Revaluation reserve	22	(15,837)	(22,759)
Property revaluation surplus		1,947	1,755
Other reserves	23	15,748	14,614
Total capital and reserves		11,873	1,291
Total liabilities, capital and reserves		320,273	260,127

The balance sheet is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 156 to 192.

INCOME STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2008
(AMOUNTS IN LEK MILLION, UNLESS OTHERWISE STATED)

	Notes	Year ended 31 December 2008	Year ended 31 December 2007 Reclassified
Operations with non-residents			
Interest and commission income	24	6,503	6,755
Interest and commission expense	25	(607)	(337)
Operations with non-residents, net		5,896	6,418
Operations with residents			
Interest and commission income	26	4,972	4,633
Interest and commission expense	27	(2,751)	(2,302)
Operations with residents, net		2,221	2,331
Other operating income, net	28	1,891	30
Net trading income	29	673	652
Profit/ (Loss) from exchange rate		4,670	(8,035)
Total income from Banking activities		15,351	1,396
Other administrative expenses			
Personnel expenses	30	(769)	(660)
Depreciation	13	(135)	(117)
Amortization	13	(84)	(69)
General and administrative expenses		(375)	(420)
Total other administrative expenses		(1,363)	(1,266)
Net income from Banking activities		13,988	130
Transfer (to)/ from revaluation reserve		(4,670)	8,035
		9,318	8,165
Provisions (Note 19)		(20)	-
Net profit before allocation		9,298	8,165
Reversal of property revaluation surplus		38	26
Distribution of profit to paid in capital		-	(1,750)
Distribution of profit to Legal Reserve		(2,334)	(1,431)
Distribution of profit to Albanian Government		(6,941)	(5,010)
Interest receivable from Government securities for covering temporary capital deficit		(61)	-
Total		9,298	8,165

The income statement is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 156 to 192.

STATEMENT OF CHANGES IN EQUITY FOR THE YEAR ENDED 31
DECEMBER 2008 (AMOUNTS IN LEK MILLION, UNLESS OTHERWISE
STATED)

	Capital	Legal reserve	Revaluation reserve	Property revaluation surplus	Other reserves	Retained earnings	Net profit	Total
As at 31 December 2006	750	3,750	(15,856)	2,660	8,706	-	-	10
Net income from Banking activity	-	-	-	-	-	-	130	130
Transfer to/ from revaluation reserves	-	-	(8,035)	-	-	-	8,035	-
Securities revaluation	-	-	1,124	-	-	-	-	1,124
Adjustment for revaluation of Property in 2006 (Note 13)	-	-	-	(1,706)	-	-	-	(1,706)
Increase in property revaluation 2007	-	-	-	827	-	-	-	827
Government funds for covering temporary capital deficit	-	-	-	-	5,908	-	-	5,908
Release of tangible fixed asset revaluation surplus	-	-	-	(26)	-	26	-	-
Other revaluation	-	-	8	-	-	-	-	8
Profit distribution (Note 20, 21)	1,750	1,431	-	-	-	(26)	(8,165)	(5,010)
As at 31 December 2007	2,500	5,181	(22,759)	1,755	14,614	-	-	1,291
Net income from Banking activity	-	-	-	-	-	-	13,988	13,988
Transfer to/ from revaluation reserves	-	-	4,670	-	-	-	(4,670)	-
Securities revaluation	-	-	2,169	-	-	-	-	2,169
Gold and Precious Metals Reserve	-	-	-	-	7,042	-	-	7,042
Property revaluation 2008 (Printing House, Note 13)	-	-	-	230	-	-	-	230
Release of government funds for covering temporary capital deficit	-	-	-	-	(5,908)	-	(61)	(5,969)
Release of tangible fixed asset revaluation surplus	-	-	-	(38)	-	38	-	-
Other revaluations	-	-	83	-	-	-	-	83
Reduction for Provisions (Note 19)	-	-	-	-	-	-	(20)	(20)
Profit distribution (Note 21)	-	2,334	-	-	-	(38)	(9,237)	(6,941)
As at 31 December 2008	2,500	7,515	(15,837)	1,947	15,748	-	-	11,873

The statement of changes in equity is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 156 to 192.

CASH FLOW STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2008
(AMOUNTS IN LEK MILLION, UNLESS OTHERWISE STATED)

	Notes	Year ended 31 December 2008	Year ended 31 December 2007 Reclassified
Cash flows from operating activities			
Net profit before allocation		9,298	8,165
Non-cash items in the statement of operation			
Interest and commission income (non-residents)		(6,503)	(6,755)
Interest and commission expense (non-residents)		607	337
Interest and commission income (residents)		(4,972)	(4,633)
Interest and commission expense (residents)		2,751	2,302
Net trading income		(673)	(652)
(Profit) / Loss from sale of available for sale investments		(1,881)	114
Gain from forward foreign exchange contracts		-	(41)
Grant amortization (deferred income)		(3)	(73)
Provision for doubtful loans		18	(2)
Depreciation and amortization		219	186
Cash flow before the movement of working capital		(1,139)	(1,052)
Changes in working capital			
Decrease in deposits with the IMF		121	831
Decrease/ (Increase) in other foreign assets		238	(37)
Decrease in transit loans		26	44
(Increase) in Government Loan		(3,000)	-
(Increase) / Decrease in other domestic assets		(491)	(122)
(Decrease) in due to the IMF		(992)	(1,313)
(Decrease) in due to financial institutions		(6)	(62)
Increase in other foreign liabilities		10	64
Increase in due to resident Banks		756	17,657
Increase/ (Decrease) in due to the Government		6,783	(1,631)
Increase/ (Decrease) in other domestic liabilities		554	(27)
Purchase of held for trading securities (in foreign currency)		(17,708)	(18,185)
Sale of held for trading securities (in foreign currency)		16,670	18,155
Cash flows generated from operations		2,961	15,374
Interest received		7,003	6,857
Interest paid		(2,834)	(2,364)
Net cash from operating activities		5,991	18,815

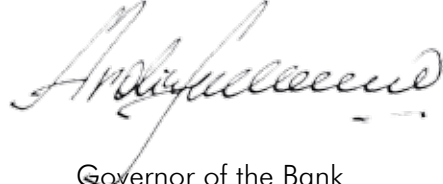
CASH FLOW STATEMENT FOR THE YEAR ENDED 31 DECEMBER 2008
(CONTINUED) (AMOUNTS IN LEK MILLION, UNLESS OTHERWISE STATED)

	Notes	Year ended 31 December 2008	Year ended 31 December 2007
Cash flows from investing activities			Reclassified
Purchase of property and equipment		(283)	(207)
Purchase of intangible assets		(278)	(15)
Purchase of available for sale investments (in foreign currency)		(338,361)	(242,240)
Purchase of available for sale investments (domestic assets)		(180,678)	(180,212)
Sale and maturity of available for sale investments (in foreign currency)		337,258	230,159
Sale and maturity of available for sale investments (domestic assets)		177,137	185,658
(Increase)/ decrease of repurchase agreement		(18,496)	3,143
Adjustment for effect of foreign exchange		883	(136)
Net cash used in investing activities		(22,818)	(3,850)
Cash flows from financing activities			
Gold and precious metals reserve		7,042	-
Increase/ (Decrease) in money in circulation emissions		45,500	(3,500)
Release of government funds for covering temporary capital deficit		(61)	-
Profit distribution		(6,941)	(5,010)
Net cash generated from / (used in) financing activities		45,540	(8,510)
Increase in cash during the year		28,713	6,455
Cash and cash equivalents at the beginning of the year	31	53,169	46,714
Cash and cash equivalents at the end of the year	31	81,882	53,169

The cash flow statement is to be read in conjunction with the notes to and forming part of the financial statements set out on pages 156 to 192.

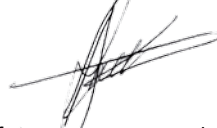
The financial statements were authorised by the Supervisory Council on 11 March 2009 and signed on its behalf by:

Ardian Fullani



Governor of the Bank

Artan Toro



Director of Accounting and
Finance Department

NOTES TO THE FINANCIAL STATEMENTS FOR THE YEAR ENDED 31
DECEMBER 2008 (AMOUNTS IN LEK MILLION, UNLESS OTHERWISE
STATED)

1. GENERAL

The Bank of Albania (the 'Bank') is the Central Bank of the Republic of Albania and was established according to the Law No. 8269, dated December 23, 1997 'On the Bank of Albania'.

Under the terms of its charter the Bank's main responsibilities are:

- formulating, adopting and executing the monetary policy of Albania, which shall be consistent with its primary objective;
- formulating, adopting and executing the exchange arrangement and the exchange rate policy of Albania;
- issuing of licenses or revoking and supervising banks that engage in the banking business in order to secure the banking system stability;
- holding and managing its official foreign reserves;
- acting as banker and adviser to, and as fiscal agent of, the Government of Republic of Albania; in order to promote an effective operation of payments systems.

The Bank is subject to the regulatory requirements of the Parliament of the Republic of Albania and the Law 'On the Bank of Albania'.

2. BASIS OF PREPARATION

(a) Statement of compliance

The financial statements have been prepared in accordance with the accounting policies adopted in the Bank's Accounting Manual approved from the order No.50 of the Council of Ministers, dated 26 January 2001 and other policies approved by the Supervisory Council of the Bank of Albania.

These accounting policies are broadly in line with International Financial Reporting Standards ('IFRS') approved by the International Accounting Standards Board ('IASB').

(b) Basis of measurement

The financial statements have been prepared on the historical cost basis except for the following:

- financial instruments at fair value through profit or loss are measured at fair value
- available-for-sale financial assets are measured at fair value

- gold is measured at fair value
- buildings are measured at revalued amount.

(c) Functional and presentation currency

These financial statements are presented in Albanian Lek ('LEK'), which is the Bank's functional currency. Except as indicated, financial information presented in LEK has been rounded to the nearest million.

(d) Use of estimates and judgments

The preparation of financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future periods affected.

Information about significant areas of estimation uncertainty and critical judgments in applying accounting policies that have the most significant effect on the amounts recognised in the financial statements are described in Note 4.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out below have been applied consistently to all periods presented in these financial statements. The most significant exception from IFRS is explained below:

IAS 39 'Financial Instruments: Recognition and Measurement'

Interest income and expenses on financial assets and liabilities are recognized in the income statement on an accrual basis, calculated on straight line basis (see Note 3.a). This method is not in accordance with IAS 39, which requires the calculation of an effective interest basis. Additionally, the borrowings from international financial institutions are recognized at cost rather than fair value as required by IAS 39.

a. Interest and commission recognition

Interest income and expense are recognized in the income statement on an accrual basis. Interest income and expense include the interest earned on coupons, as well as the amortization of any discount or premium or other differences between the initial carrying amount of an interest bearing instrument and its amount at maturity calculated on a straight line basis.

Interest income and expense on all trading assets and liabilities are considered to be incidental to the Bank's trading operations and are presented

together with all other changes in the fair value of trading assets and liabilities in net trading income.

Fee and commission income and expenses arise on financial services provided by the Bank and are recognized when the corresponding service is provided. Other operating income/expense includes gains and losses arising from disposals and changes in the fair value of available for sale assets.

b. Foreign currency transactions

Transactions in foreign currencies are recorded at the rates of exchange prevailing at the dates of the transactions. At each balance sheet date, monetary items denominated in foreign currencies are retranslated at the rates prevailing at the balance sheet date. Some non-monetary items that are measured in terms of historical cost in a foreign currency are not retranslated.

Exchange differences are initially recognized in profit or loss in the period in which they arise, and are then transferred to 'Revaluation reserves' in capital, according to the Law No. 8269, dated 23 December 1997 'On the Bank of Albania'.

The applicable official Bank rate (LEK to the foreign currency unit) for the principal currencies as at 31 December 2008 and 2007 were as below:

	31 December 2008	31 December 2007
United States dollar (USD)	87.91	82.89
European Union currency unit (EUR)	123.80	121.78
British pound (GBP)	127.66	166.02
Special Drawing Rights (SDR)	136.07	130.84
Japanese yen (JPY)	0.9743	0.7401
Gold ('XAU') per 1 onz	76,042.15	69,337.49

c. Net trading income

Net trading income comprises gains less loss related to trading assets and liabilities, and includes all realised and unrealised fair value changes, interest, and foreign exchange differences.

d. Lease payments made

Payments made under operating leases are recognised in profit or loss on a straight-line basis over the term of the lease. Lease incentives received are recognised as an integral part of the total lease expense, over the term of the lease.

e. Taxation and Profit distribution policy of the Bank

The Bank is not subject to income tax based on the law 'On the Bank of Albania'.

The Bank's policy of distribution of profit from banking operations is defined in the Law 'On the Bank of Albania'. According to this law, the Bank allocates all the realized profit to the State Budget after having fulfilled its requirement for reserve fund as required from the Supervisory Council of the Bank.

According to Article 64, point (a) of the Law 'On the Bank of Albania', the net gain / losses arising from the revaluation of assets and liabilities denominated in foreign currencies, is transferred to the equity on a revaluation reserve account 'Revaluation reserves'. According to Article 64, point (b), the Government of Albania issues debt securities at market interest rates to cover the negative balance of the revaluation reserve arising from Bank's activity.

According to the requirements of Article 9 of the Law 'On the Bank of Albania', the Bank sets aside 25 per cent of the net profit for the year into a Legal Reserve until the reserve amounts to 500% of the capital (see accounting policy 3.f).

According to Article 11 of the Law 'On the Bank of Albania' no transfer, redemption or payment under Articles 8, 9 or 10 of this law shall be made if the assets of the Bank are less than the sum of its liabilities and paid-up capital. Under such conditions, based on the 'On the Bank of Albania' under article 7, the Ministry of Finance might have to transfer to the Bank interest bearing negotiable government securities, in such amount as would be necessary to remedy the deficiency.

f. Legal reserve

According to the requirements of Article 9 of the Law 'On the Bank of Albania', the Bank sets aside 25 per cent of the net profit for the year into a Legal Reserve until the reserve amounts to 500% of the capital. Subsequent to the allocation of reserves as required by the Law 'On the Bank of Albania', the Bank stipulates the remainder to be paid into the State Budget.

g. Financial assets and liabilities

(i) Recognition

All financial assets held-to-maturity, or financial assets available-for-sale are initially recognised on the settlement date. The investments held-for-trading are accounted for on the trade date. The Bank initially recognises loans and advances, deposits, and financial liabilities on the date at which they are originated.

A financial asset or financial liability is initially measured at cost.

(ii) Classification

See accounting policies 3(h), (i), (j) and (k).

(iii) Derecognition

The Bank derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or when it transfers the rights to receive the contractual cash flows on the financial asset in a transaction in which substantially all the risks and rewards of ownership of the financial asset are transferred. Any interest in transferred financial assets that is created or retained by the Bank is recognised as a separate asset or liability.

The Bank derecognises a financial liability when its contractual obligations are discharged or cancelled or expire. The Bank writes off certain loans and investment securities when they are determined to be uncollectible (see note 4).

(iv) Offsetting

Financial assets and liabilities are set off and the net amount presented in the balance sheet when, and only when, the Bank has a legal right to set off the amounts and intends either to settle on a net basis or to realise the asset and settle the liability simultaneously.

Income and expenses are presented on a net basis only when permitted by the accounting standards, or for gains and losses arising from a group of similar transactions such as in the Bank's trading activity.

(v) Fair value measurement

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction on the measurement date. When available, the Bank measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

For investments traded in organized financial markets, fair value is determined by reference to stock exchange quoted market bid prices at the close of business on the balance sheet date. For investments where there is no quoted market price, a reasonable estimate of the fair value is determined by reference to the current market value of another instrument, which is substantially the same.

(vi) Identification and measurement of impairment

At each balance sheet date the Bank assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the future cash flows of the asset that can be estimated reliably.

Financial assets, other than those 'Held for trading', are assessed for indicators of impairment at each balance sheet date. Financial assets are impaired where there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial asset, the estimated future cash flows of the investment have been impacted. For financial assets carried at amortized cost, the amount of the impairment is the difference between the asset's carrying amount and the present value of estimated future cash flows, as follows:

- For loans originated by Bank – the recoverable amount of originated loans is calculated based on the year-end evaluations of loans, including the accrued interest. In determining the recoverable amounts of loans to employees, management considers the particular factors, including the review of repayment history of the debt by its former employees. The provision for impairment losses on loans is reported in the income statement as a charge and is deducted from the relevant asset category on the balance sheet. When it is determined that a loan cannot be recovered, all the necessary legal procedures have been completed and the final loss has been determined, the loan is written off.
- For financial assets held to maturity – the carrying amount of the asset is reduced to its estimated recoverable amount either directly or through the use of an allowance account and the amount of the loss is included in the statement of profit and loss.
- For financial assets available for sale –when a decline in the fair value of an available-for-sale financial asset has been recognized directly in equity and there is objective evidence that the asset is impaired, the cumulative loss that had been recognized directly in equity shall be removed from equity and recognized in profit or loss even though the financial asset has not been derecognized.

(vii) Securities lending agreements

Investments lent under securities lending agreements are reported in the balance sheet and are valued in accordance with the accounting policies applicable to assets held for trading and assets available-for-sale. Investments lent under securities lending agreements continue to be recognized in the Bank's balance sheet. The Bank receives cash or securities collateral for such lendings. Income arising from the securities lending agreements is reported as interest income.

h. Cash and cash equivalents

Cash and cash equivalents include notes and coins on hand and current accounts and time deposits with original maturities of less than three months. These assets are carried at amortised cost in the balance sheet.

For the purposes of the cash flow statement, the Bank includes gold and precious metals as part of cash and cash equivalents (See accounting policy 3.l).

i. Trading assets and liabilities

Trading assets and liabilities are those assets and liabilities that the Bank acquires or incurs principally for the purpose of selling or repurchasing in the near term, or holds as part of a portfolio that is managed together for short-term profit or position taking.

Trading assets and liabilities are initially recognised at cost and subsequently measured at fair value in the balance sheet with transaction costs taken directly to profit or loss. All changes in fair value are recognised as part of net trading income in profit or loss. Trading assets and liabilities are not reclassified subsequent to their initial recognition.

j. Available for sale investments

Investment securities are initially measured at cost. Available-for-sale investments are subsequently carried at fair value. Interest income is recognised in profit or loss on an accrual basis.

Fair value changes are recognised directly in equity until the investment is sold or impaired, whereupon the cumulative gains and losses previously recognised in equity are recognised in profit or loss.

k. Loans and advances

Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Bank does not intend to sell immediately or in the near term.

When the Bank purchases a financial asset and simultaneously enters into an agreement to resell the asset (or a substantially similar asset) at a fixed price on a future date ("reverse repo"), the arrangement is accounted for as a loan or advance, and the underlying asset is not recognised in the Bank's financial statements.

Loans and advances are initially measured at cost. Interest income is recognised in profit or loss on an accrual basis.

l. Gold and other precious metals

Gold and other precious metals are valued at market value based on the official London Bullion Market price at the balance sheet date.

m. Property and equipment

(i) Recognition and measurement

Items of property and equipment are measured at cost less accumulated depreciation and accumulated impairment losses, except for the buildings, which are stated at revalued amount, calculated using the replacement cost method.

Any revaluation increase arising on the revaluation of buildings is credited in equity to the property revaluation reserve, except to the extent that it reverses a revaluation decrease for the same asset previously recognized in profit or loss, in which case the increase is credited to profit or loss to the extent of the decrease previously charged. A decrease in the carrying amount arising on the revaluation of such land and buildings is charged to profit or loss to the extent that it exceeds the balance, if any, held in the properties revaluation reserve relating to a previous revaluation of that asset. Cost includes expenditures that are directly attributable to the acquisition of the asset.

(ii) Subsequent costs

The cost of replacing a part of an item of property or equipment is recognised in the carrying amount of the item if it is probable that the future economic benefits embodied within the part will flow to the Bank and its cost can be measured reliably. The carrying amount of the replaced part is derecognised. The costs of the day-to-day servicing of property and equipment are recognised in profit or loss as incurred.

(iii) Depreciation

Depreciation is recognised in profit or loss on a straight-line basis over the estimated useful lives of each part of an item of property and equipment. Land is not depreciated.

The estimated useful lives for the current and comparative periods are as follows:

- | | |
|-------------------------------------|--------------|
| • Buildings, Head Office | 40 years |
| • Buildings, branches | 25 years |
| • Vehicles | 5 - 10 years |
| • Furniture, fixtures and equipment | 3 - 20 years |

Depreciation methods, useful lives and residual values are reassessed at the reporting date.

n. Intangible assets**(i) Printing and minting costs**

The costs of printing banknotes and minting coins are capitalized as intangible assets and amortized over 2.5 years and 10 years, respectively.

(ii) Software

Software acquired by the Bank is stated at cost less accumulated amortisation and accumulated impairment losses.

Subsequent expenditure on software assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is expensed as incurred.

Amortisation is recognised in profit or loss on a straight-line basis over the estimated useful life of the software, from the date that it is available for use. The estimated useful life of software is two years.

o. Impairment of non-financial assets

The carrying amounts of the Bank's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists then the asset's recoverable amount is estimated.

An impairment loss is recognised if the carrying amount of an asset exceeds its recoverable amount.

The recoverable amount of an asset is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a discount rate that reflects current market assessments of the time value of money and the risks specific to the asset.

Impairment losses recognised in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

p. Grants

Grants are recognised initially as deferred income when there is reasonable assurance that they will be received and the Bank will comply with the conditions associated with the grant. Grants that compensate the Bank for expenses incurred are recognised in profit or loss on a systematic basis in the same periods in which the expenses are recognised. Grants that compensate the Bank for the cost of an asset are recognised in profit or loss on a systematic basis over the useful life of the asset.

q. Loans from the International Monetary Fund (IMF)

Borrowings from the IMF are denominated in Special Drawing Rights.

r. Repurchase agreements

When the Bank sells a financial asset and simultaneously enters into an agreement to repurchase the asset (or a similar asset) at a fixed price on a future date ("repo"), the arrangement is accounted for as a deposit, and the underlying asset continues to be recognised in the Bank's financial statements.

Repurchase agreements are initially measured at cost. Repurchase agreements are included in 'Due to domestic Banks'. Based on the Bank's regulation on repurchase agreements, the Bank is not required to put up any collateral for these securities.

Interest earned on reverse repurchase agreements and interest incurred on repurchase agreements is recognized as interest income or interest expense, over the life of each agreement using the interest rate approved by the Supervisory Council of the Bank of Albania.

s. Provisions

A provision is recognised if, as a result of a past event, the Bank has a present legal or constructive obligation that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation.

t. Employee benefits

(i) Defined contribution plans

Obligations for contributions to defined contribution pension plans are recognised as an expense in profit or loss when they are due.

The Bank makes compulsory social security contributions that provide pension benefits for employees upon retirement. The local authorities are responsible for providing the legally set minimum threshold for pensions in Albania under a defined contribution pension plan.

(ii) Termination benefits

Termination benefits are recognised as an expense when the Bank is demonstrably committed, without realistic possibility of withdrawal, to a formal detailed plan to either terminate employment before the normal retirement date, or to provide termination benefits as a result of an offer made to encourage voluntary redundancy. Termination benefits for voluntary redundancies are recognised if the Bank has made an offer of voluntary redundancy, it is probable that the offer will be accepted, and the number of acceptances can be estimated reliably.

(iii) Short-term benefits

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A provision is recognised for the amount expected to be paid under short-term cash bonus if the Bank has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be estimated reliably.

u. Comparative information

When necessary, comparative figures are reclassified for the purposes of comparability. At 31 December 2007, the Bank included in net interest and commission income and Other operating income, net, a net amount of LEK 652 million, relating to net trading income. This amount was presented as net trading income in the income statement for the year ended 31 December 2008. In addition, certain amounts that had been included in 'Net cash used in financing activities', which did not relate to physical flow of cash were reclassified to non-cash movements within 'Cash flows from operating activities'.

4. USE OF ESTIMATES AND JUDGEMENTS

These disclosures supplement the commentary on financial risk management (see note 36).

Key sources of estimation uncertainty Allowances for credit losses

Assets accounted for at cost are evaluated for impairment on a basis described in accounting policy 3(g)(vi).

The specific counterparty component of the total allowances for impairment applies to financial assets evaluated individually for impairment and is based upon management's best estimate of the present value of the cash flows that are expected to be received. In estimating these cash flows, management makes judgements about counterparty's financial situation and the net realisable value of any underlying collateral. Each impaired asset is assessed on its merits, and estimate of cash flows considered recoverable are independently approved.

Determining fair values

The determination of fair value for financial assets and liabilities for which there is no observable market price requires the use of valuation techniques. For financial instruments that trade infrequently and have little price transparency, fair value is less objective, and requires varying degrees of judgement depending on liquidity, concentration, uncertainty of market factors, pricing assumptions and other risks affecting the specific instrument. See also "Valuation of financial instruments" below.

Accounting judgements in applying the Bank's accounting policies

Accounting judgements made in applying the Bank's accounting policies include:

Printing House

At 31 December 2007 the Bank controlled the operations of the Printing House, a business entity engaged in the printing of Government high security material and publications of Bank of Albania. The Bank did not consolidate the financial operations of the Printing House due to its unclear status related to the ownership with the Government of Albania.

The activity of the Printing House was terminated on 30 September 2008, based on the Decision of the Council of Ministers No.598 dated 5 September 2007 'On the termination of the economic and financial activities of the Printing House of the Bank of Albania', amended by Decision No. 862 dated 18 June 2008 (see Note 32).

Valuation of financial instruments

Fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. For all other financial instruments the Bank determines fair values using valuation techniques. Valuation techniques include net present value and discounted cash flow models, comparison to similar instruments for which market observable prices exist and other valuation models. The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date that would have been determined by market participants acting at arm's length.

The Bank uses widely recognised valuation models for determining the fair value of common and more simple financial instruments that use only observable market data and require little management judgment and estimation. Observable prices and model inputs are usually available in the market for listed securities. Availability of observable market prices and model inputs reduces the need for management judgment and estimation and also reduces the uncertainty associated with determination of fair values. Availability of observable market prices and inputs varies depending on the products and markets and is prone to changes based on specific events and general conditions in the financial markets.

For more complex instruments, the Bank uses proprietary valuation models, which usually are developed from recognised valuation models. Some or all of the significant inputs into these models may not be observable in the market, and are derived from market prices or rates or are estimated based on assumptions. Valuation models that employ significant unobservable inputs require a higher degree of management judgment and estimation in determination of fair value. Management judgment and estimation are

usually required for selection of the appropriate valuation model to be used, determination of expected future cash flows on the financial instrument being valued, determination of probability of counterparty default and prepayments and selection of appropriate discount rates.

5. GOLD AND PRECIOUS METALS

	31 December 2008	31 December 2007
Gold – foreign	5,265	923
Gold and precious metals - domestic	2,462	63
Total	7,727	986

As at 31 December 2008, the value of gold owned by the Bank placed in gold time deposits and current accounts abroad was LEK 5,265 million (2007: LEK 923 million).

Other gold and precious metals included within domestic assets include non-monetary gold, platinum and silver held in a domestic vault, valued at the London fixing rate on the balance sheet date, amounting to LEK 2,462 million as at 31 December 2008 (2007: LEK 63 million).

The negative difference of LEK 301 million (2007: positive difference of LEK 126 million) resulting from the revaluation of gold is recorded in the revaluation reserve.

The increase in gold and precious metals was based on Law No. 9862, and dated 24 January 2008 'On the transfer of ownership of gold and other precious metals from the Albanian Council of Ministers to the ownership of the Bank of Albania'. After its approval the Law was published in the Official Gazette No.10, dated 13 February 2008 and has become effective on 27 February 2008. The value of Gold and Precious Metals Reserve is equivalent to LEK 7,042 million (Note 23) and is valued at market value based on the official London Bullion Market price on 27 February 2008.

6. DEPOSITS WITH THE INTERNATIONAL MONETARY FUND

	31 December 2008	31 December 2007
International Monetary Fund (IMF)	6,269	6,868
Special Drawing Rights (SDR)	639	160
Accrued interest	2	3
Total	6,910	7,031

Deposits with the IMF resulted from the membership of the Republic of Albania in the IMF, according to Law No.8269 dated 23 December 1997 'On the Bank of Albania'. These deposits have as counterparty accounts due to the IMF (see Note 14).

The Special Drawing Rights (SDR) represents deposits placed with the International Monetary Fund. The SDR holdings bear interest, which is determined on a weekly basis. The interest rate prevailing as at 31 December 2008 was 0.82% p.a. (2007 – 3.5 % p.a.).

7. DEPOSITS WITH NON RESIDENT BANKS

	31 December 2008	31 December 2007
Current accounts	53,509	9,472
Short-term deposits	5,292	31,369
Accrued interest	23	135
Total	58,824	40,976

Short-term deposits and current accounts earn interest at rates mostly based on the currency of the deposit or current account. The interest rate of overnight deposits is 0.01% p.a.

8. INVESTMENTS IN FOREIGN CURRENCY

8.1 AVAILABLE FOR SALE INVESTMENTS

The portfolio of available for sale investments in foreign currency is disclosed using market value as follows:

	31 December 2008	31 December 2007
Foreign Governments treasury notes	75,473	89,821
Bank for International Settlements (BIS): medium-term investments	39,011	26,448
Fixed rate investments (FIX BIS)	8,723	6,432
Agencies' treasury bills	5,269	-
Agencies' notes	3,863	1,395
Total	132,339	124,096

Foreign Government treasury notes have coupon rates varying between 0.875% and 9% (2007: 2.05% and 9%). Interest is paid semi-annually (USD and GBP) and annually (EUR) and maturities vary between April 2009 and June 2021. The yields vary between 0.74% and 5.81% (2007: 2.95% and 5.8%).

Bank for International Settlements – medium term investments comprised of fixed coupon securities denominated in EUR, USD and GBP with coupon rates varying between 2.5% and 5.85% (2007: 2.5% and 4.7%). Interest is payable annually for investments in EUR and semi-annually for investments in GBP and USD, and maturities range between March 2009 and March 2014. The yields vary between 2.84% and 5.88% (2007: 3.3% and 5.95%).

Fixed rate investments (FIX BIS) issued by the Bank for International Settlements are denominated in EUR and JPY with yields that vary between 0.11% and 4.51% (2007: 0.32% and 4.39%) and maturities range between February 2009 and June 2009.

Agencies notes are denominated in USD with coupon rates between 2.75% and 4.75% (2007: 3.25% and 7.12 %). Interest is paid semi-annually and maturities range between December 2009 and December 2010. The yield is between 2.11% and 3.26% (2007: 4.24% and 5.2%).

Agencies Treasury Bills are denominated in USD with yields that vary between 1.93% and 3.01% and maturities vary between March 2009 and July 2009.

8.2. HELD FOR TRADING INVESTMENTS

Held for trading portfolio in foreign currency measured at market value is presented as follows:

	31 December 2008	31 December 2007
Government treasury notes	5,667	5,818
Agencies notes	4,752	2,929
Government treasury bills	195	-
Total	10,614	8,747

Government treasury notes, denominated in USD, have coupon rates varying between 1.125% and 7.5% (2007: 3.37% and 6%). Interest is paid semi-annually and maturities range between November 2009 and November 2017.

Agencies notes are denominated in USD with fixed coupon rates varying between 2.25% and 5% (2007: 4.12% and 5.37%) and floating rates varying between 0.56% and 4.59% (2007: no floating rates investments held). Interest payments vary from monthly to annual, and maturities range between September 2009 and February 2012.

Government zero-coupon treasury bills are denominated in USD and maturities range between November 2009 and December 2009.

Starting from 25 July 2006 this portfolio is administrated from International Bank for Reconstruction and Development (IBRD) as stated in the agreement 'On the administration and technical assistance on investing the foreign reserve of Bank of Albania (Reserves and Advisory Management Program) signed between Bank of Albania and IBRD on 23 September 2005. Investments from this portfolio are accounted for on the trade date.

9. OTHER ASSETS (IN FOREIGN CURRENCY)

	31 December 2008	31 December 2007
Quotas in international financial institutions		
International Bank for Reconstruction and Development subscriptions (IBRD)	355	353
International Development Agency subscriptions (IDA)	12	12
Multilateral Investment Guarantee Agency subscriptions (MIGA)	6	6
International Finance Corporation subscriptions (IFC)	65	61
European Bank for Reconstruction and Development subscriptions (EBRD)	52	48
Islamic Development Bank subscriptions (IDB)	20	19
Total Quotas	510	498
Cash on hand in foreign currency	1,067	4
Receivables from IBRD	-	250
Total	1,577	752

As at 31 December 2008, other foreign assets are comprised of subscriptions for participation of the Bank of Albania in International Financial Institutions of LEK 510 million (2007: LEK 498 million), (see Note 33) and cash on hand in foreign currency of LEK 1,067 million (2007: LEK 4 million).

Receivables from IBRD represent the amount of cash to be received from the sale of securities administrated from IBRD, during the period within the trading date and settlement date (refer to note 8.2).

10. LOANS DISBURSED TO THIRD PARTIES

10.1. TRANSIT CREDITS

The total of LEK 69 million (2007: LEK 95 million) represent credits for services provided to the former Italian-Albanian Bank (Intesa SanPaolo Bank) for further distribution to ultimate borrowers to support state development programs.

This loan has not been secured by any collateral.

10.2. LOANS TO ALBANIAN GOVERNMENT

The loan to Albanian Government of LEK 3,000 million is a short-term loan with an interest rate of 7.44% per annum. The maturity date is 2 February 2009.

10.3. LOANS TO RESIDENT BANKS

Loans to resident banks represent reverse repurchase agreements signed between the Bank of Albania and second-tier banks in amount of LEK 20,072 million (2007: LEK 1,509 million), with maturing terms between one week and three months (2007: one week). On 31 December 2008 the interest rate of reverse repurchase agreement varies from 6.25% to 7.65% (2007: 6.25%).

11. AVAILABLE FOR SALE INVESTMENT (DOMESTIC ASSETS)

	31 December 2008	31 December 2007
Short-term treasury bills	74,594	66,523
Total	74,594	66,523

Short-term treasury bills as at 31 December 2008 relate to Government of Albania zero-coupon treasury bills, with short-term maturity, ranging between January 2009 and December 2009, with yields varying between 6.05% and 8.65% (2007: 6% and 7.94%).

12. INVESTMENTS IN LOCAL CURRENCY

On 31 December 2007 the Ministry of Finance issued a security with a price of LEK 5,909 million (nominal value of LEK 6,000 million), bearing interest equal to the treasury bills yield of the last quarter, and maturity date on 27 March 2008 with a call option conditional to the transfer of Gold from the Albanian Government.

The Ministry of Finance transferred to the Bank the above mentioned interest bearing negotiable government securities because as of 31 December 2007 the Bank's total of paid up capital and liabilities exceeded assets by LEK 7,118 million. The securities were issued based on Article 7, of the Law 'On the Bank of Albania' No.8269, dated 23 December 1997 for the purpose of remedying the above mentioned deficiency. Following the transfer of gold ownership to the Bank of Albania on 27 February 2008, the Ministry became eligible to withdraw the securities.

13. OTHER DOMESTIC ASSETS

	31 December 2008	31 December 2007
Property and equipment, net	2,645	2,263
Intangible assets, net	305	111
Loans to employees	1,167	1,037
Other debtors	333	3
Numismatic	38	40
Inventory	48	38
Other	11	11
Total	4,547	3,503

On 31 December 2008, the Bank has included within the category 'Land, building and general constructions' as part of property and equipment, the value of the Printing House building. The revaluation method used was the replacement cost method which showed a revalued amount of the building of LEK 234 million, from a net book value of LEK 4 million. The revaluation increase of LEK 230 million was credited directly to the Revaluation reserve

in Equity. In this category is also included the value of branch buildings reconstructed in 2008 with a value of LEK 176 million.

On 31 December 2007 the Bank used an independent valuer to revalue the buildings of Bank of Albania, included in the category 'Land, building and general constructions'. The revaluation method was the replacement cost method with a revalued amount of LEK 1,938 million, from a net book value of the class of buildings of LEK 1,179 million. The increase to the revaluation of LEK 826 million was credited directly to the Revaluation reserve in Shareholder's Equity, with a decrease in revaluation of LEK 69 million included under 'General expenses of the Bank'.

Effective 26 December 2006 a revaluation of the head quarter building was performed by an independent appraiser based on capitalization of rental income and selling prices for new business centers in neighborhood which raised a revaluation surplus of LEK 1,706 million. The tangible assets (buildings) of the bank have been revalued using the replacement cost method based on the requirement of IAS 16 'Property, Plant and Equipment'. The reversal of this transaction is recorded in the financial statements of the Bank for the year ending 31 December 2007.

Loans to employees include a provision for legal claims of LEK 10 million at 31 December 2008 (2007: LEK 10 million).

Loans to employees are collateralised by security such as mortgages, totaling approximately LEK 1,352 million at 31 December 2008 (2007: LEK 1,218 million).

The net book values of property and equipment by category at 31 December 2008 are comprised of:

	Land, buildings and general constructions	General equipment	Transport vehicles	Work in Progress	Total
Cost / Valuation					
Balance at 1 January 2008	1,942	778	241	48	3,009
Additions	264	77	12	164	517
Transfers	176	-	-	(176)	-
Balance at 31 December 2008	2,382	855	253	36	3,526
Accumulated depreciation					
Balance at 1 January 2008	-	576	170	-	746
Charge for the year	45	74	16	-	135
Balance at 31 December 2008	45	650	186	-	881
Net carrying amount					
Balance at 31 December 2008	2,337	205	67	36	2,645
Balance at 31 December 2007	1,942	202	71	48	2,263

The net book values of property and equipment by category at 31 December 2007 are comprised of:

	Land, buildings and general constructions	General equipment	Transport vehicles	Work in Progress	Total
Cost / Valuation					
Balance at 1 January 2007	2,964	710	200	33	3,907
Additions	6	121	41	39	207
Disposals	-	(53)	-	-	(53)
Transfers	24	-	-	(24)	-
Reversal of revaluation in 2006	(1,706)	-	-	-	(1,706)
Reversal of the elimination of revaluation 2006	189	-	-	-	189
Revaluation of the bank buildings	758	-	-	-	758
Eliminated on revaluation	(293)	-	-	-	(293)
Balance at 31 December 2007	1,942	778	241	48	3,009
Accumulated depreciation					
Balance at 1 January 2007	69	560	155	-	784
Charge for the year	35	67	15	-	117
Disposals	-	(51)	-	-	(51)
Reversal of the elimination of the revaluation in 2006	189	-	-	-	189
Eliminated on revaluation	(293)	-	-	-	(293)
Balance at 31 December 2007	-	576	170	-	746
Net carrying amount					
Balance at 31 December 2007	1,942	202	71	48	2,263
Balance at 31 December 2006	2,895	150	45	33	3,123

The net book values of intangible assets by category at 31 December 2008 are comprised of:

	Computer software	Banknotes printed and coins minted	Total intangible assets
Cost / Valuation			
Balance at 1 January 2008	353	2,453	2,806
Additions	24	254	278
Balance at 31 December 2008	377	2,707	3,084
Accumulated amortization			
Balance at 1 January 2008	338	2,357	2,695
Charge for the year	14	70	84
Balance at 31 December 2008	352	2,427	2,779
Net carrying amount			
Balance at 31 December 2008	25	280	305
Balance at 31 December 2007	15	96	111

The net book values of intangible assets by category at 31 December 2007 are comprised of:

	Computer software	Banknotes printed and coins minted	Total intangible assets
Cost / Valuation			
Balance at 1 January 2007	338	2,454	2,792
Additions	15	-	15
Disposals	-	(1)	(1)
Balance at 31 December 2007	353	2,453	2,806
Accumulated amortization			
Balance at 1 January 2007	314	2,312	2,626
Charge for the year	24	45	69
Balance at 31 December 2007	338	2,357	2,695
Net carrying amount			
Balance at 31 December 2007	15	96	111
Balance at 31 December 2006	24	142	166

14. DUE TO THE INTERNATIONAL MONETARY FUND

	31 December 2008	31 December 2007
Poverty Reduction and Growth Facility ('PRGF')	6,116	6,821
IMF securities account	4,871	5,042
IMF account in LEK	1,878	2,077
Accrued interest	4	6
Total	12,869	13,946

PRGF borrowings related to the Republic of Albania's IMF quotas and were drawn down on behalf of the Government for macroeconomic reforms. These loans are compounded from the following component facilities:

The loan 'Poverty Reduction and Growth Facility 2' was approved from the agreement dated 13 May 1998 totaling SDR 45,040,000 and was drawn down during the period 1999 to 2001. The outstanding balance as at 31 December 2008 was SDR 11,241,400 (2007: SDR 19,660,900), equivalent of LEK 1,530 million (2007: LEK 2,573 million). This facility is repayable by 2011 in 10 semi-annual installments commenced in 2004. Interest is payable, at 0.5% semi-annually.

The loan 'Poverty Reduction and Growth Facility 3' is approved from the agreement dated 21 June 2002 totaling SDR 28,000,000 and the last disbursement was made on 20 June 2005. The balance as of 31 December 2008 is SDR 26,400,000 (2007: SDR 27,600,000), equivalent of LEK 3,592 million (2007: LEK 3,611 million), with an interest rate of 0.5% payable semi-annually. This facility is repayable after a grace period of five and a half years in 10 semi-annual equal installments.

The loans 'Poverty Reduction and Growth Facility 4 (PRGF 4)' and 'Extended Fund Facility' are approved from a three year agreement signed on 27 January

2006 in amount of SDR 17,045,000. The disbursement of two entrenchments of PRGF 4 loan in the amount of SDR 1,217,500 each, was made during 2008, with a semi annual interest payable of 0.5% and the balance as of 31 December 2008 is SDR 7,305,000 (2007: SDR 4,870,000), equivalent of LEK 994 million (2007: LEK 637 million). This facility is repayable after a grace period of five and a half years in 10 semiannual equal installments.

Included in the IMF accounts in LEK is the loan 'Extended Fund Facility' (EFF) of LEK 936 million (2007: LEK 690 million). The loan was disbursed during the period 2006 - 2008 and is the equivalent of SDR 7,305,000 (2007: 4,870,000). The facility is repayable after a grace period of four and a half years and will be repaid within 10 years. The interest on these loans is floating and payable each three months. As at 31 December 2008 the interest rate was 1.84% (2007: 4.77%).

15. DUE TO NON-RESIDENT FINANCIAL INSTITUTIONS

	31 December 2008	31 December 2007
Transit credits (Note 8.1)	69	95
Loan from the Republic of Greece	1,090	1,072
Due to the World Bank	14	12
Accrued interest	5	4
Total	1,178	1,183

Transit credit of LEK 69 million represents the outstanding loan received from the European Investment Bank and is compounded from EUR 0.5 million (Note 8.1). Interest is paid by the recipients of these transit credits (Banks and domestic companies) directly to the providers of the funds.

The loan from the Republic of Greece in amount of EUR 8.8 million was granted for the purpose of funding the balance of payments of the Republic of Albania. The interest rate is 1.17% per annum, payable semi-annually. The loan matures in 2018.

Due to the World Bank represents the accounts of international organizations such as International Bank for Reconstruction and Development (IBRD), International Development Agency (IDA), Multilateral Investment Guarantee Agency (MIGA) in the Bank of Albania.

16. CURRENCY IN CIRCULATION

The exclusive rights of issuing national currency are vested with the Bank. This item comprises valid domestic banknotes and coins in circulation issued by the Bank.

The following Bank notes and coins were in circulation as at 31 December 2008 and 2007:

Nominal value LEK	31 December 2008		31 December 2007	
	Number in thousand	Total LEK (million)	Number in thousand	Total LEK (million)
100	4,121	412	5,906	591
200	16,022	3,204	13,183	2,637
500	61,830	30,915	52,883	26,441
1,000	84,030	84,030	69,202	69,202
2,000	502	1,004	-	-
5,000	16,349	81,744	12,074	60,368
Coins		2,404		1,923
		203,713		161,162

17. DUE TO RESIDENT BANKS

	31 December 2008	31 December 2007
Foreign currency		
Compulsory reserve	26,583	23,848
Accounts of second-tier banks	77	1,964
	26,660	25,812
Domestic currency (LEK)		
Compulsory reserve	34,316	32,837
Accounts of second-tier banks	1,668	3,148
Overnight deposits	5,120	5,211
	41,104	41,196
Accrued interest	39	43
Total	67,803	67,051

Interest on compulsory reserves is calculated as follows:

- LEK balances: 70% of the yield on the repurchase agreements: 4.375% as at 31 December 2008 (70% of the yield on the repurchase agreements: 4.375% as at 31 December 2007);
- USD balances: 70% of the Federal Bank rate: 0.7% as at 31 December 2008 (70% of the one-month USD LIBOR rate: 3.40% as at 31 December 2007);
- EUR balances: 70% of the European Bank rate: 2.28 % as at 31 December 2008 (70% of the one-month EUR LIBOR rate: 3.11% as at 31 December 2007).

Overnight deposits from domestic banks bear an interest of 4.5% (2007: 4.5%).

18. DUE TO THE GOVERNMENT

	31 December 2008	31 December 2007
Profit to be distributed to the Government	1,741	-
Deposits received on behalf of the Government	19,335	14,280
Other	20	33
Total	21,096	14,313

Deposits received on behalf of the Government in the amount of LEK 19,335 million, include the main account of LEK 6,408 million, international donor funds deposited at the Bank for subsequent transfer to aid projects in Albania, of LEK 2,029 million, an amount of LEK 2,503 million representing a reserve fund account of the government on behalf of the Social Insurance Institute and Health Insurance Institute and other funds for other financing activities in the amount of LEK 8,395 million.

'Other' includes funds received by the Bank of LEK 20 million (2007: 19 million) from a loan granted to the Government by the Islamic Arabian Bank of Development.

19. OTHER DOMESTIC LIABILITIES

	31 December 2008	31 December 2007
Due to Printing House (Note 32)	-	215
Deposits of individuals from the participation in Treasury Bills	891	586
Net Pension fund obligation	-	6
Due to financial institutions	206	16
Due to third parties (Note 32)	239	-
Other	144	104
Total	1,480	927

Pension plan scheme consists of employee contribution of 2% of gross salary and employer contribution of 15% on the total payroll amount. On 31 December 2008 the amount of pension funds assets invested in treasury bills maturing within 12 months, is LEK 272 million (2007: LEK 391 million) and the amount invested in treasury bills maturing within 5-7 years, is LEK 302 million (2007: LEK 69 million).

Total amount of contributions paid from the Bank's employees till 31 December 2008 is LEK 43 million (2007: LEK 35 million) and the total amount of contributions paid from the Bank till 31 December 2008 is LEK 359 million (2007: LEK 302 million). The movements in such contributions and changes in net assets available for pension fund benefits are as follows:

	31 December 2008	31 December 2007
Assets at 1 January	466	372
Income from investment		
Interest	43	31
Net income from investment	43	31
Employees contribution	8	12
Employer contribution	57	51
Total contribution	65	63
Net increase	108	94
Assets at 31 December	574	466
Liabilities at 31 December	574	472
Net obligation	-	6

Third party transactions of LEK 239 million consist of capital, reserves and the retained earnings from the activity of the printing house from its closure until the end of the financial year 2008. The transactions with the printing house as at 30 September 2008 amounted to ALL 230 million (Note 32), and by the end of the year assets with a total value of LEK 5 million were transferred to the Bank of Albania. There were also expenses incurred of LEK 15 million and liabilities paid to third parties of LEK 19 million.

'Other' includes accrued expenses of LEK 75 million (2007: LEK 54 million) related to maintenance of ATM system, AIPS (clearing system), services for statistical information, commission for managing the foreign reserve by IBRD, SWIFT etc. Also included are provisions for several litigations raised in the normal course of business. The provision at 31 December 2008 is LEK 39 million (2007: LEK 21 million).

Movements in the provisions for litigations are as follows (See Note 28):

	Year ended 31 December 2008	Year ended 31 December 2007
Balance at the beginning of the period	21	19
Additional provision for the period	20	8
Provision reversal for the period	(2)	(6)
Balance at the end of the period	39	21

The additional provision for the year ended 31 December 2008 was recognized in equity.

20. CAPITAL

Based on the requisition No.9852 of the Ministry of Finance dated 28 December 2007 and based on the decision of the Supervisory Council No.4 dated 23 January 2008 the capital of the Bank was increased by LEK 1,750 million.

21. LEGAL RESERVE

Following the increase in the Bank's capital and according to the Law 'On the Bank of Albania', at the end of each financial year the Bank shall allocate an amount equivalent to 25 percent of the net profits for that year to the general reserve until the General Reserve Fund amounts to 500 percent of the paid-up capital of the Bank of Albania.

A decision for the increase in the paid in capital of the Bank was taken on 28 December 2007 and for this purpose the Bank could not increase legal reserve to the limit of 25% of the net profits, but transferred an amount of LEK 1,431 million. In 2008 the Bank transferred an amount of LEK 2,334 million to the legal reserve.

22. REVALUATION RESERVE

The components of the revaluation reserve are as follows:

	31 December 2008	31 December 2007
Revaluation of foreign currency and gold balances	(18,870)	(23,540)
Security revaluation reserve	2,916	747
Revaluation of historic notes and coins	117	34
Total	(15,837)	(22,759)

During 2008, the net gain arising from the revaluation of foreign currency and gold balances was LEK 4,670 million (2007: net loss of LEK 8,035 million).

The revaluation of securities to market value during the year ended 31 December 2008 resulted in a gain of LEK 2,169 million (2007: gain of LEK 1,124 million).

In accordance with the Law 'On the Bank of Albania' Article 64, point (a), the net gain / losses arising from the revaluation of assets and liabilities denominated in foreign currencies, is transferred to equity on a revaluation reserve account 'Revaluation of foreign currency balances'.

Pursuant to the above article, point (b), during the year 2008 the Ministry of Finance issued securities of LEK 23,540 million (2007: Lek 15,505 million), to cover the negative balance of the revaluation reserve arising from Bank's activity to the end of year 2007. These securities have a renewable maturity of six months (see Note 33).

The total amount of LEK 23,540 million covers the loss for the period 2003 to 2007.

23. OTHER RESERVES

The components of other reserves are as follows:

	31 December 2008	31 December 2007
Special reserve for Balance of Payments	7,209	7,209
Government funds for covering the temporary capital deficit (Note 12)	-	5,908
Reserve of gold and precious metals (Note 5)	7,042	-
Investment fund	301	301
Other	1,196	1,196
Total	15,748	14,614

The special reserve for the Balance of Payments relates to funds provided by the European Community as financial assistance to support Albania in its transition towards the market economy. These grants have been transferred during the period 1992 – 1993 supporting the long-standing of the Balance

of Payment and reserves balance and no movement have been incurred in this reserve since 1995.

Investment fund consists of a fund created with decision of Supervisory Council with the aim to purchase a new building for the Bank of Albania.

'Other' includes reserves created from the allocation of profits for years 2002 - 2007 based on the Supervisory Council decisions in the respective following years.

24. INTEREST AND COMMISSION INCOME (NON - RESIDENTS)

	Year ended 31 December 2008	Year ended 31 December 2007
		Reclassified
Interest income from securities	4,492	5,040
Interest income from time deposits	1,587	1,145
Interest from SDR deposits with IMF	29	33
Other (discounts)	395	537
Total	6,503	6,755

25. INTEREST AND COMMISSION EXPENSE (NON -RESIDENTS)

	Year ended 31 December 2008	Year ended 31 December 2007
Amortization of premium on securities	499	222
Interest expenses on loans of foreign institutions	13	13
Interest expenses on IMF accounts	64	69
Other	31	33
Total	607	337

26. INTEREST AND COMMISSION INCOME (RESIDENTS)

	Year ended 31 December 2008	Year ended 31 December 2007
Interest income from securities	4,571	4,362
Interest income from Government loans	-	6
Income from repurchase and reverse repurchase agreements	351	227
Other	50	38
Total	4,972	4,633

27. INTEREST AND COMMISSION EXPENSE (RESIDENTS)

	Year ended 31 December 2008	Year ended 31 December 2007
Interest expense on compulsory reserve	2,270	1,915
Interest expenses on REPO agreements	103	140
Interest expenses on Government deposits	206	184
Other	172	63
Total	2,751	2,302

28. OTHER OPERATING INCOME/(EXPENSES), NET

	Year ended 31 December 2008	Year ended 31 December 2007
		Reclassified
Net profit/(loss) from the sale of available for sale investments	1,881	(114)
Grant depreciation	3	73
Provision for legal claims and other (note 19)	-	(8)
Other	7	38
Net profit from forward contracts	-	41
Total	1,891	30

29. NET TRADING INCOME

	Year ended 31 December 2008	Year ended 31 December 2007
		Reclassified
Interest income from trading assets	337	396
Gains less loss related to sale of trading assets	307	41
Unrealized fair value changes	29	215
Total	673	652

30. PERSONNEL EXPENSES

Personnel expenses consist of employee salaries, social insurance, pension plan contribution and other costs.

Social costs represent mainly compulsory contributions to the Social Security Fund. As at 31 December 2008, the Bank had 418 employees (2007: 391 employees).

31. CASH AND CASH EQUIVALENTS

	31 December 2008	31 December 2007
Deposits with foreign banks (Note 7)	58,801	40,841
Domestic currency on hand	14,287	11,338
Foreign currency on hand (Note 9)	1,067	4
Gold held abroad (Note 5)	5,265	923
Gold and other precious metals held domestically (Note 5)	2,462	63
Total	81,882	53,169

32. PRINTING HOUSE

As detailed in Note 4, at 31 December 2007 the Bank controlled the operations of the Printing House. The activity of the Printing House was terminated on 30 September 2008, based on the Decision of the Council of Ministers No.598 dated 5 September 2007 'On the termination of the

economic and financial activities of the Printing House of the Bank of Albania', amended by Decision No. 862 dated 18 June 2008.

According to points 7 and 8 of Decision No. 598, the inventory and intangible assets of the Printing House were transferred to the Ministry of Finance, and the machinery used in the printing of fiscal stamps was transferred to the Tax Office. According to point 10 of the same decision the ownership of the Buildings of the Printing House was transferred to the Bank.

Following termination, the Bank has included in 'Other domestic liabilities' (see Note 19) an amount of LEK 230 million (2007: LEK 215 million), which represents the amounts payable to the Printing House at termination date (see below the Receivables from the Bank balances), plus an additional amount of LEK 9 million (2007: nil), which represents other transfers between the Bank and Printing House upon termination. These transfers were based on the above mentioned decisions. The Bank has not yet taken a decision on the settlement of the total liabilities of LEK 239 million.

The financial position of the Printing House as at 30 September 2008 (termination date) and 31 December 2007 is set out below:

	30 September 2008	31 December 2007
Assets		
Tangible assets	5	6
Inventory	45	49
Receivables from the Bank	230	215
Total Assets	280	270
Equity		
Initial capital	51	51
Legal reserve	19	19
Investment reserves	24	24
Other reserves	6	6
Retained earnings	179	169
Total equity	279	269
Other liabilities	1	1
Total liabilities and equity	280	270

	Nine-months ended 30 September 2008	Year ended 31 December 2007
Revenue	57	52
Expenses	(46)	(51)
Profit for the year	11	1

33. CONTINGENCIES AND COMMITMENTS

The Bank maintains certain accounts in foreign currencies related to agreements concluded between the Government of Albania and foreign governments and financial organizations. These accounts have not been included within the Bank's balance sheet.

(i) Participation in International Financial Institutions

In the past the Republic of Albania has subscribed to a number of subscriptions in International Financial Institutions, including International Bank for Reconstruction and Development ('IBRD'), International Development Agency, Multilateral Investment Guarantee Agency ('MIGA'), International Finance Corporation, European Bank for Reconstruction and Development ('EBRD') and Islamic Development Bank. As detailed in Note 9, 'Other Assets (In Foreign Currency)', the Bank has paid an amount of LEK 510 million (2007: Lek 499 million).

The total amount of paid in subscriptions confirmed by IBRD, MIGA and EBRD as at 31 December 2008 was LEK 820 million (2007: LEK 793 million), of which LEK 412 million (2007: LEK 409 million) was paid by Bank of Albania and included in the balance sheet. An amount of LEK 402 million (2007: LEK 379 million), which was paid by the Albanian Government and an amount of LEK 6 million (2007: LEK 5 million) of paid in subscriptions in Multilateral Investment Guarantee Agency, which are supported by promissory notes, are not included in the Bank's balance sheet.

The total amount of callable subscription to support the Republic of Albania, confirmed by IBRD, and MIGA as at 31 December 2008 was LEK 8,565 million (2007: LEK 8,075 million).

The Bank and the Government of Albania have not signed a Memorandum of Understanding for the purpose of allocating the original contributions and ownership of the subscriptions in the International Financial Institutions between both parties.

(ii) Treasury bills issued by the Albanian Ministry of Finance

On 31 December 2008 treasury bills issued by the Ministry of Finance for the purpose of covering the revaluation reserve created during the period 2003 - 2007 in amount of LEK 23,540 million has a renewable maturity of six months.

34. MANAGED ASSETS

As at 31 December 2008, the Bank held as custodian short-term treasury bills, at nominal value LEK 237 billion, and government bonds with maturity 2 up to 7 years at nominal value LEK 145 billion. These securities are issued by the Albanian Government.

At as 31 December 2008, gold and other precious metals of Albanian Government held in custody from Bank of Albania is nil (2007: LEK6,129 million).

35. RELATED PARTIES

Parties are considered to be related if one party has the ability to control the other party or exercise significant influence over the party in making financial and other decisions.

In considering each possible related party relationship, attention is directed to the substance of the relationship and not merely the legal form.

The only related parties of Bank of Albania are the relations with directors and the members of the Supervisory Council. As at 31 December 2008 and 2007 transactions made with related parties comprised:

	31 December 2008	31 December 2007
Loans to directors		
- Directors	132	110
Total assets	132	110

The loans have an interest rate of 0.5% and are repayable after a grace period of two years within 30 years by monthly equal installments. The home loans are collateralized:

	Year ended 31 December 2008	Year ended 31 December 2007
Administrative expenses		
- Mobile expenses		
- Directors and Supervisory Council Members	5	4
- Salaries and Bonuses		
- Directors and Supervisory Council Members	101	90
- Bank contribution to pension plan scheme		
- Directors	8	7
Total of administrative expenses	114	101

36. FINANCIAL RISK MANAGEMENT

(a) Risk management framework

The Supervisory Board has overall responsibility for the establishment and oversight of the Bank's risk management framework.

The foreign reserve is under the administration of the Bank of Albania and its investment is performed by the Monetary Operations Department, which is based on the regulation 'On foreign reserve management policy', approved by the Supervisory Board. Its investment strategy depends mainly on the specific function of a central bank which is strictly regulated and in accordance with the requirements of the Law 'On the Bank of Albania'.

The reserve, in accordance with the liquidity needs, is invested in short-term securities and in fixed coupon instruments. The remaining portion is held in SDRs, and in monetary gold.

The Bank has exposure to the following risks from financial instruments:

- liquidity risk
- credit risk
- market risks
- operational risks

This note presents information about the Bank's exposure to each of the above risks, the Bank's objectives, policies and processes for measuring and managing risk.

(b) Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in meeting obligations associated with its financial liabilities.

Management of liquidity risk

Policies to monitor and address liquidity risk are set by the Supervisory Council of the Bank. The Bank manages its liquidity risk by investing in short term deposits with foreign banks and in debt securities in liquid and serious markets.

The Bank's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under both normal and stressed conditions, without incurring unacceptable losses or risking damage to the Bank's reputation, and to comply with its monetary and exchange policy. The portfolio is defined annually based on the forecasts of the monthly and annual liquidity needs for each currency. The investments in securities are considered as sufficiently liquid instruments.

Because of the specifics of a central bank, the Bank is not exposed to liquidity risk in relation to liabilities in local currency.

The following table shows the Bank's financial liabilities on the basis of their contractual maturity and the financial assets on the basis of their earliest possible expected maturity. The Bank's expected cash flows on these instruments may vary from this analysis.

31 December 2008	Up to one Month	One to three Months	Three to six months	Six months to one year	One to five years	Over five years	Total
Due to IMF	361	118	281	476	4,266	7,367	12,869
Due to non-resident financial institutions	-	-	-	-	69	1,109	1,178
Other foreign liabilities	261	-	-	-	-	-	261
Currency in circulation	203,713	-	-	-	-	-	203,713
Due to resident Banks	67,803	-	-	-	-	-	67,803
Due to the Government	21,096	-	-	-	-	-	21,096
Other domestic liabilities	589	-	-	891	-	-	1,480
Total Liabilities 2008 (contractual maturity date)	293,823	118	281	1,367	4,335	8,476	308,400
Total assets 2008 (expected maturity date)	113,428	36,821	41,838	33,601	83,169	11,416	320,273

31 December 2007	Up to one Month	One to three Months	Three to six months	Six months to one year	One to five years	Over five years	Total
Due to IMF	218	139	347	555	4,324	8,363	13,946
Due to non-resident financial institutions	-	-	-	-	95	1,088	1,183
Other foreign liabilities	251	-	-	-	-	-	251
Currency in circulation	161,162	-	-	-	-	-	161,162
Due to resident Banks	67,051	-	-	-	-	-	67,051
Due to the Government	14,313	-	-	-	-	-	14,313
Domestic liabilities & deferred income	930	-	-	586	-	-	930
Total Liabilities 2007 (contractual maturity date)	243,339	139	347	1,141	4,419	9,451	258,836
Total assets 2007 (expected maturity date)	68,789	39,789	29,076	15,286	96,769	10,418	260,127

(c) Credit risk

Credit Risk is the risk of the decrease in value of the foreign currency reserve as result of insolvency of a financial institution or the bankruptcy or insolvency of a debt issuer, in whose debt instruments the Bank has invested its own funds.

The investment limits of the Bank set a system of limits of maximum exposures to individual financial institutions and debt issuers. The set limits are calculated on the basis of credit ratings of the counterparty. The internal credit rating is based on criteria which are approved by the Supervisory Council. Credit risk is also mitigated through the diversification of the portfolio.

Loans to domestic Banks are secured by Albanian Government Treasury bills.

The financial assets which represent credit risk at the balance sheet date are shown below:

Assets	2008	2007
Gold - foreign (Note 5)	5,265	923
Special Drawing Rights with IMF (Note 6)	639	160
Deposits with non-resident banks (Note 7)	58,824	40,976
Available for sale investments (foreign currency) (Note 8.1)	132,339	124,096
Held-for-trading investment (foreign currency) (Note 8.2)	10,614	8,747
Loans to Government (Note 10.2)	3,000	-
Loans to resident banks (note 10.3)	20,072	1,509
Available for sale investments - domestic (Note 11)	74,594	66,523
Investments in local currency (Note 12)	-	5,909
Total assets	305,347	248,843

An analysis of concentrations of financial assets by type of counterparty at the balance sheet date is shown below:

Credit rating	Gold	Special Drawing Rights with IMF	Deposits with non-resident banks	Available for sale investments (foreign currency)	Held-for-trading investment (foreign currency)	Loan to Government	Loans to domestic banks	Available for sale investments (domestic assets)	Total
Central bank	4,436	639	17,620	-	-	-	-	-	22,695
BIS Basle	-	-	37,474	47,734	-	-	-	-	85,208
Foreign Government & Agencies Securities	-	-	-	84,605	10,614	-	-	-	95,219
Commercial Banks	829	-	3,730	-	-	-	-	-	4,559
Albanian Government B1	-	-	-	-	-	3,000	-	74,594	77,594
Unrated	-	-	-	-	-	-	20,072	-	20,072
Total 31 December 2008	5,265	639	58,824	132,339	10,614	3,000	20,072	74,594	305,347

The Albanian Government is rated based on the Standard & Poor's ratings or equivalents.

Credit rating	Gold	Special Drawing Rights with IMF	Deposits with non-resident banks	Available for sale investments (foreign currency)	Held-for-trading investment (foreign currency)	Loans to domestic banks	Investments in local currency	Available for sale investments (domestic assets)	Total
Central Banks	923	160	11,730	-	-	-	-	-	12,813
BIS Basle	-	-	1,173	32,880	-	-	-	-	34,053
Commercial Banks	-	-	28,073	-	-	-	-	-	28,073
Foreign Government & Agencies Securities	-	-	-	91,216	8,747	-	-	-	99,963
Albanian Government B1	-	-	-	-	-	-	5,909	66,523	72,432
Unrated	-	-	-	-	-	1,509	-	-	1,509
Total 31 December 2007	923	160	40,976	124,096	8,747	1,509	5,909	66,523	248,843

An analysis of concentrations of credit risk by geographic location is shown below:

	Europe	USA	Republic of Albania	Other	Total
Gold - foreign	5,265	-	-	-	5,265
Special Drawing Rights with IMF	-	-	-	639	639
Deposits with non-resident banks	53,521	5,303	-	-	58,824
Available for sale investments (foreign currency)	101,600	30,739	-	-	132,339
Held-for-trading investment (foreign currency)	-	10,614	-	-	10,614
Loans to Government	-	-	3,000	-	3,000
Loans to resident banks	-	-	20,072	-	20,072
Available for sale investments - domestic	-	-	74,594	-	74,594
31 December 2008	160,386	46,656	97,666	639	305,347

	Europe	USA	Republic of Albania	Other	Total
Gold - foreign	923	-	-	-	923
Special Drawing Rights with IMF	-	-	-	160	160
Deposits with non-resident banks	37,346	3,630	-	-	40,976
Available for sale investments (foreign currency)	90,060	34,036	-	-	124,096
Held-for-trading investment (foreign currency)	-	8,747	-	-	8,747
Loans to resident banks	-	-	1,509	-	1,509
Available for sale investments - domestic	-	-	66,523	-	66,523
Investments in local currency	-	-	5,909	-	5,909
31 December 2007	128,329	46,413	73,941	160	248,843

(d) Market risk

Market risk is the risk that changes in market prices, such as interest rates, equity prices, foreign exchange rates and credit spreads (not relating to changes in the obligor's / issuer's credit standing) will affect the Bank's income or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising the return on risk.

The key elements of price risk affecting the Bank are:

- currency risk associated with fluctuations in the fair value of financial instruments due to changes in foreign exchange rates; and
- interest rate risk associated with fluctuations in the fair value of financial instruments due to changes in market interest rates.

The Bank's exposure to currency risk is monitored on a continual basis by the Monetary Operations Department. Financial assets denominated in foreign currencies are disclosed in each relevant note to the financial statements.

Interest rate risk

The Bank's operations are subject to the risk of interest rate fluctuations which affect the prices of interest-earning assets (including investments) and interest-bearing liabilities. The primary objective of the Bank is the prices' stability; hence the monetary policy of the Bank is guided by this objective. The Monetary Operations Department of the Bank monitors interest rate risk. The Bank mitigates such risks by maintaining a significant excess of interest bearing assets over liabilities. The Bank maintains a portfolio of interest bearing financial assets and liabilities such that the net interest income is significantly higher than operating needs, in order to minimize the potential adverse effects of interest rate fluctuations. Interest rates applicable to financial assets and liabilities are disclosed in each relevant note to the financial statements. The assets and liabilities with floating interest rates involve the risk of changes in the base which serves to determine the interest rates. Floating rate instruments are detailed as follows:

31 December 2008	Average rate	Six to twelve months	One to five years	Over five years	Total
Assets					
Held for trading investments	2.6%	439	533	-	972
Total		439	533	-	972
Liabilities					
Due to the IMF	1.84%	-	-	936	936
Total		-	-	936	936
Floating Interest gap		439	533	(936)	36
Sensitivity to 100 b.p. increase		4	5	(9)	-
31 December 2007					
Liabilities					
Due to the IMF	4.77%	-	-	690	690
Total		-	-	690	690
Floating Interest gap		-	-	(690)	(690)
Sensitivity to 100 b.p. increase		-	-	(7)	(7)

A summary of the Bank's interest-earning assets and interest-bearing liabilities (including the floating rate instruments above) by maturity dates as at 31 December 2008 and 2007 is as follows:

	Up to one month	One to three months	Three to six months	Six to twelve months	One to five years	Over five years	Non-interest earning/bearing	Total
Assets								
Gold and precious metals	829	-	-	-	-	-	4,436	5,265
Deposits with the IMF	639	-	-	-	-	-	6,271	6,910
Deposits with non residents Banks	58,801	-	-	-	-	-	23	58,824
Available for sale investments	-	8,183	17,892	29,038	74,264	2,962	-	132,339
Held for trading investments	-	-	-	1,282	8,836	496	-	10,614
Other foreign assets	-	-	-	-	-	-	1,577	1,577
Gold and precious metals	-	-	-	-	-	-	2,462	2,462
Transit Credits	-	-	-	-	-	-	69	69
Loan to Albanian Government	-	3,000	-	-	-	-	-	3,000
Loans to resident banks	14,566	5,438	-	-	-	-	68	20,072
Available for sale investments	27,167	20,200	23,946	3,281	-	-	-	74,594
Other domestic assets	-	-	-	-	-	1,177	3,370	4,547
Total	102,002	36,821	41,838	33,601	83,100	4,635	18,276	320,273
Liabilities and equity								
Due to the IMF	361	118	281	476	4,266	1,550	5,817	12,869
Due to non-resident institutions	-	-	-	-	-	1,090	88	1,178
Other foreign liabilities	261	-	-	-	-	-	-	261
Currency in circulation	-	-	-	-	-	-	203,713	203,713
Due to resident Banks	67,764	-	-	-	-	-	39	67,803
Due to the Government	-	-	-	-	-	-	21,096	21,096
Other domestic liabilities	206	-	-	-	-	-	1,274	1,480
Capital and reserves	-	-	-	-	-	-	11,873	11,873
Total	68,592	118	281	476	4,266	2,640	243,900	320,273
Gap as at 31 December 2008	33,410	36,703	41,557	33,125	78,834	1,995	(225,624)	-
Cumulative gap - 2008	33,410	70,113	111,670	144,795	223,629	225,624	-	-

	Up to one month	One to three months	Three to six months	Six to twelve months	One to five years	Over five years	Non-interest earning/bearing	Total
Assets								
Gold and precious metals	-	-	-	-	-	-	923	923
Deposits with the IMF	160	-	-	-	-	-	6,871	7,031
Deposits with non residents Banks	32,961	7,880	-	-	-	-	135	40,976
Available for sale investments	3,705	6,646	9,479	13,679	88,586	2,001	-	124,096
Held for trading investments	-	-	-	659	8,088	-	-	8,747
Other foreign assets	250	-	-	-	-	-	502	752
Gold and precious metals	-	-	-	-	-	-	63	63
Transit credits	-	-	-	-	-	-	95	95
Loan to resident banks	1,508	-	-	-	-	-	1	1,509
Available for sale investments	26,650	19,328	19,597	948	-	-	-	66,523
Investments in local currency	-	5,909	-	-	-	-	-	5,909
Other domestic assets	-	-	-	-	-	1,048	2,455	3,503
Total	65,234	39,763	29,076	15,286	96,674	3,049	11,045	260,127
Liabilities and equity								
Due to the IMF	218	139	347	555	4,324	1,928	6,435	13,946
Due to non-resident institutions	-	-	-	-	-	1,072	111	1,183
Other foreign liabilities	251	-	-	-	-	-	-	251
Currency in circulation	-	-	-	-	-	-	161,162	161,162
Due to resident Banks	61,896	-	-	-	-	-	5,155	67,051
Due to the Government	-	-	-	-	-	-	14,313	14,313
Deferred income	-	-	-	-	-	-	3	3
Other domestic liabilities	-	-	-	-	-	-	927	927
Capital and reserves	-	-	-	-	-	-	1,291	1,291
Total	62,365	139	347	555	4,324	3,000	189,397	260,127
Gap as at 31 December 2007	2,869	39,624	28,729	14,731	92,350	49	(178,352)	-
Cumulative gap - 2007	2,869	42,493	71,222	85,953	178,303	178,352	-	-

Exchange rate risk

Currency risk exists where there is a difference between the currency structure of assets and that of liabilities. From an accounting point of view, the Bank is exposed to currency risk when conducting transactions in financial instruments denominated in currencies other than the Bank's base currency.

The foreign currency reserve structure is determined by the currency structure of the liabilities of the Central bank and the Government. The main foreign currency reserves are in EUR and USD.

	LEK	USD	EURO	GBP	Other	Total
Assets						
Gold and precious metals	-	-	-	-	5,265	5,265
Deposits with the IMF	5,812	-	-	-	1,098	6,910
Deposits with non residents Banks	-	10,536	39,865	1,023	7,400	58,824
Available for sale investments	-	38,867	81,270	7,329	4,873	132,339
Held for trading investments	-	10,614	-	-	-	10,614
Other foreign assets	335	616	625	-	1	1,577
Gold and precious metals	2,462	-	-	-	-	2,462
Transit Credits	-	-	69	-	-	69
Loan to Albanian Government	3,000	-	-	-	-	3,000
Loans to resident banks	20,072	-	-	-	-	20,072
Available for sale investments	74,594	-	-	-	-	74,594
Other domestic assets	4,211	2	334	-	-	4,547
Total assets	110,486	60,635	122,163	8,352	18,637	320,273
Liabilities						
Due to the IMF	6,749	-	-	-	6,120	12,869
Due to non-resident financial institutions	14	-	1,164	-	-	1,178
Other foreign liabilities	-	261	-	-	-	261
Currency in circulation	203,713	-	-	-	-	203,713
Due to resident banks	41,133	6,172	20,498	-	-	67,803
Due to the Government	9,345	248	11,503	-	-	21,096
Other domestic liabilities	1,454	19	7	-	-	1,480
Total liabilities	262,408	6,700	33,172	-	6,120	308,400
Net currency position as at 31 December 2008	(151,922)	53,935	88,991	8,352	12,517	11,873
Net currency position as at 31 December 2007	(134,948)	50,563	72,351	9,816	3,509	1,291

	LEK	USD	EURO	GBP	Other	Total
Assets						
Gold and precious metals	-	-	-	-	923	923
Deposits with the IMF	6,429	-	-	-	602	7,031
Deposits with non residents Banks	-	8,286	27,552	1,514	3,624	40,976
Available for sale investments	-	39,969	70,638	8,303	5,186	124,096
Held for trading investments	-	8,747	-	-	-	8,747
Other foreign assets	335	415	2	-	-	752
Gold and precious metals	63	-	-	-	-	63
Transit Credits	-	-	95	-	-	95
Loans to resident banks	1,509	-	-	-	-	1,509
Available for sale investments	66,523	-	-	-	-	66,523
Investments in local currency	5,909	-	-	-	-	5,909
Other domestic assets	3,497	2	4	-	-	3,503
Total assets	84,265	57,419	98,291	9,817	10,335	260,127
Liabilities						
Due to the IMF	7,120	-	-	-	6,826	13,946
Due to non-resident financial institutions	11	-	1,172	-	-	1,183
Other foreign liabilities	-	251	-	-	-	251
Currency in circulation	161,162	-	-	-	-	161,162
Due to resident banks	41,225	6,274	19,552	-	-	67,051
Due to the Government	8,797	310	5,205	1	-	14,313
Deferred income	3	-	-	-	-	3
Other domestic liabilities	895	21	11	-	-	927
Total liabilities	219,213	6,856	25,940	1	6,826	258,836
Net Position as at 31 December 2007	(134,948)	50,563	72,351	9,816	3,509	1,291
Net Position as at 31 December 2006	(132,642)	52,343	73,612	9,753	(3,056)	10

(e) Operational risk

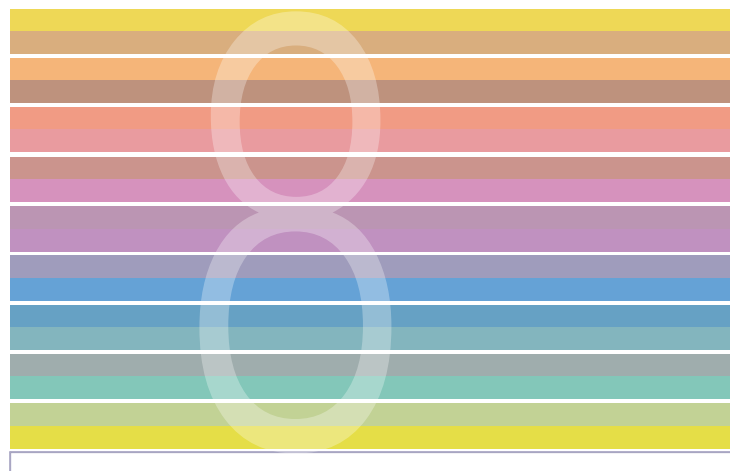
Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Bank's processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the Bank's operations.

Operational risk management is supported by the development of overall Bank standards for the management of operational risk and a wide range of common policies, staff management regulations, obligatory requirements, and the internal control systems on several activities of the Bank.

37. SUBSEQUENT EVENTS

There are no significant events after the balance sheet date that may require adjustment or disclosure in the financial statements.

*STATISTICAL
APPENDIX*



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1. PRICES, OUTPUT AND LABOUR MARKETS

1.1 CONSUMER PRICE INDEX (Indexes)

	CPI Total December 2007 = 100												
		Food and non-alcoholic beverages	Alcoholic beverages and tobacco	Clothing and footwear	Rent, water, fuel and power	Furniture household and maintenance	Medical care	Transport	Communication	Recreation and culture	Education service	Hotels, coffee-house and restaurants	Goods and various services
	1	2	3	4	5	6	7	8	9	10	11	12	13
2005 ¹⁾	92.8	92.2	85.1	103.1	90.7	101.7	97.0	93.6	102.7	101.1	92.4	92.1	98.1
2006	95.0	93.2	89.9	100.3	95.3	100.4	100.3	96.8	101.9	102.1	97.7	94.3	99.2
2007	97.8	95.9	98.5	99.3	99.5	100.0	99.8	97.3	100.0	101.5	100.3	97.6	99.5
2008	101.1	100.9	100.7	96.5	103.3	100.1	100.8	104.7	94.4	103.5	100.3	101.0	100.4
2008 January February March April May June July August September October November December	100.5	101.0	100.0	98.7	100.4	100.2	100.4	100.5	100.0	100.1	100.0	100.3	100.1
	101.5	103.6	100.1	98.1	100.1	100.2	100.8	100.9	100.0	100.1	100.1	100.4	100.3
	102.4	104.3	100.3	97.4	103.9	100.2	100.8	101.7	100.0	100.4	100.0	100.5	100.4
	102.0	103.5	100.3	97.1	103.7	100.1	100.8	101.7	99.9	100.0	100.0	100.4	100.3
	101.0	100.7	100.0	96.8	103.7	100.1	100.8	103.6	99.9	99.9	100.0	100.4	100.3
	100.2	98.1	99.9	96.7	103.3	100.2	100.7	107.8	99.9	99.8	100.1	100.4	100.3
	99.6	96.5	99.9	95.3	103.3	100.0	100.6	109.8	99.9	99.7	100.1	100.5	100.3
	100.2	98.0	100.3	94.9	103.6	100.0	100.7	109.1	99.9	100.1	100.1	100.8	100.3
	101.3	100.1	101.6	95.1	104.2	100.1	101.0	108.6	90.8	110.4	100.5	101.2	100.4
	101.3	100.9	101.6	95.4	104.3	100.2	101.1	106.9	80.8	110.4	100.9	102.2	100.6
	101.3	101.0	101.5	96.0	104.5	100.1	101.1	104.2	80.8	110.3	101.1	102.3	100.8
	102.2	103.5	102.3	96.1	104.9	100.1	101.1	101.1	101.2	80.7	110.2	101.1	102.3

Source: INSTAT

1) The Consumer Price Index yearly data (for this and consecutive years), represent yearly average consumer price indexes by main groups. Monthly data represent consumer price Index.

1.2 YEAR ON YEAR CONSUMER PRICE INDEX, MAIN GROUPS (In percentage)

	CPI Total December 2007=100	Food and non-alcoholic beverages	Alcoholic beverages and tobacco	Clothing and footwear	Rent, water, fuel and power	Furniture household and maintenance	Medical care	Transport	Communication	Recreation and culture	Education service	Hotels, coffee- house and restaurants	Goods and various services
2005 ¹⁾	2.0	-1.9	1.5	-3.4	9.0	-1.7	7.0	5.1	-0.2	0.0	8.0	2.8	0.7
2006	2.5	0.2	12.1	-2.8	7.0	-0.9	1.2	1.1	-2.5	1.3	3.8	1.8	1.9
2007	3.1	5.4	4.0	0.1	1.0	-0.1	0.0	2.8	0.0	-2.6	-0.7	5.2	0.5
2008	2.2	3.5	2.3	-3.9	4.9	0.1	1.1	1.2	-19.3	10.2	1.1	2.3	1.1
2008 ²⁾ January	3.0	5.0	3.7	-0.7	1.4	0.0	1.0	4.3	0.0	-2.5	-0.8	5.5	0.7
February	3.6	6.5	3.6	-1.2	1.1	0.1	1.3	4.8	0.0	-2.4	-0.2	5.2	1.0
March	4.6	7.7	3.7	-1.8	4.8	0.0	1.3	5.6	0.0	-2.2	-0.3	5.0	1.1
April	4.4	7.6	3.1	-2.4	4.5	-0.1	1.3	5.2	-0.1	-2.1	-0.3	4.4	1.2
May	4.2	7.1	2.2	-2.7	4.5	0.1	0.8	7.5	-0.1	-2.0	-0.3	3.3	1.2
June	4.0	6.1	1.1	-2.6	4.1	0.3	0.7	12.4	-0.1	-2.1	-0.1	3.1	0.6
July	3.7	5.6	0.9	-3.8	3.6	0.2	0.6	14.3	-0.1	-2.3	0.0	2.9	0.7
August	2.5	2.9	0.9	-3.8	3.9	0.1	0.6	10.9	-0.1	-2.2	0.0	2.6	0.7
September	2.7	2.9	1.4	-3.9	4.4	0.0	1.2	10.8	-9.2	10.3	0.0	2.2	0.8
October	2.8	4.1	1.5	-3.9	4.5	0.2	1.1	9.1	-19.2	10.7	0.7	2.9	1.2
November	2.6	4.0	1.5	-3.8	4.6	0.0	1.1	5.3	-19.3	10.7	0.9	2.4	1.4
December	2.2	3.5	2.3	-3.9	4.9	0.1	1.1	1.2	-19.3	10.2	1.1	2.3	1.1

Source: INS/AT

1) Yearly data (for this and consecutive years), measure the variation of december index of year n with december index of year n-1.

2) Monthly data (for this and consecutive years) measure yearly index changes in percentage.

1.3 PRODUCER PRICE INDEX AND CONSTRUCTION COST INDEX (Index)

	PPI Index Total 2005=100	Producer price index, excluding construction			Construction cost index
		Mining and quarrying industry	Manufacturing industry	Electricity, gas and water supply	Total 4-th quarter 1999=100
	1	2	3	4	5
2005 ¹⁾	100.0	100.0	100.0	100.0	122.3
2006	100.1	108.7	100.7	94.5	123.7
2007	104.2	114.1	110.4	91.1	126.8
2008 ²⁾ Q I	110.0	120.9	112.9	91.5	127.3
Q II	111.5	117.5	114.7	91.5	128.3
Q III	111.7	124.7	114.4	91.5	128.8
Q IV					129.0

Source: INSTAT

1) Annual data (and consecutive years data) represent yearly average producer price indexes.

2) Quarterly data (and consecutive quarters' data) represent producer price indexes by economic activities.

1.4 YEAR ON YEAR CHANGES OF PRODUCER PRICE INDEX AND CONSTRUCTION COST INDEX. (In percentage)

	PPI Total 2005=100	Producer price index, excluding construction			Construction cost index ²⁾
		Mining and quarrying industry	Manufacturing industry	Electricity, gas and water supply	Total 4-th quarter 1999=100
	1	2	3	4	5
2005	5.1	4.5	4.9	7.2	1.4
2006	0.1	8.7	0.7	-5.5	1.1
2007	4.1	5.0	9.6	-3.6	2.5
2008 ¹⁾ Q I	7.4	5.56	6.78	0.85	0.7
Q II	7.4	2.96	6.92	0.84	1.3
Q III	7.1	9.69	6.09	0.00	1.5
Q IV					1.4

Source: INSTAT

1) Quarterly data of producer price index (for this and consecutive quarters) measure the change of current quarter with the same quarter of the previous year.

2) Annual average changes of construction cost index.

1.5 GROSS DOMESTIC PRODUCT BY EXPENDITURE APPROACH (In billion Lek)

	Gross domestic product (by expenditure approach)														Change in inventories & statistical discrepancy
	Domestic demand				Final consumption				Net export			Goods and services imports (f.o.b)			
	1 = 2 + 8 + 11	2 = 3 + 7	3 = 4 + 5 + 6	Final consumption of households	Final consumption of general government	Consumption of NPISHs	Gross fixed capital formation	Net export		Goods and services exports (f.o.b)	Goods and services imports (f.o.b)				
								8 = 9 - 10	9						
1996	346,403	442,922	369,642	337,561	31,852	229	73,279	-72,151	38,782	110,934	-24,367				
1997	346,198	443,090	372,151	336,678	35,167	306	70,939	-84,626	33,739	118,365	-12,267				
1998	409,209	505,182	419,152	376,824	41,987	340	86,030	-97,362	44,376	141,738	1,389				
1999	471,578	545,403	437,004	389,573	47,023	408	108,399	-77,321	74,588	151,910	3,497				
2000	523,043	615,863	449,879	399,935	49,454	490	165,984	-105,583	93,453	199,036	12,764				
2001	583,369	695,596	471,816	410,448	60,667	700	223,780	-119,983	107,524	227,507	7,755				
2002	622,711	771,573	535,551	465,180	69,572	800	236,021	-154,037	122,044	276,081	5,175				
2003	694,098	878,374	597,453	520,954	75,585	914	280,921	-171,642	141,290	312,931	-12,635				
2004	750,785	947,566	668,187	584,659	82,484	1,044	279,378	-168,169	165,097	333,265	-28,612				
2005	814,797	1,025,525	724,171	634,471	88,508	1,192	301,354	-200,824	185,970	386,794	-9,904				
2006 ¹⁾	891,000	1,102,927	789,752	696,492	91,889	1,371	313,175	-208,087	219,970	428,057	-3,839				

Source: INSTAT.

1) Preliminary data.

1.6 VALUE ADDED BY ECONOMIC ACTIVITY (In billion Lek)

	Growth domestic product (by economic activity)											Tax on products (-) less subsidies	
	Gross value added (basic prices)							Financial intermediation services indirectly measured (-)					
	1 = 2 + 8	2 = 3 + 4 + 5 + 6 - 7	Agriculture, hunting and forestry	Industry	Construction	Total services						7	8
			3	4	5	6	7	GDP(in current prices in billion Lek)					
1996	346,403	324,861	121,757	32,835	17,011	161,317					8,058		21,542
1997	346,198	319,588	104,506	28,973	20,172	177,085					11,148		26,610
1998	409,209	363,515	110,782	28,322	19,335	225,808					20,731		45,694
1999	471,578	424,067	114,997	32,320	26,943	271,232					21,424		47,512
2000	523,043	463,971	122,908	37,529	39,979	282,063					18,508		59,072
2001	583,369	523,613	128,039	39,449	56,450	317,570					17,895		59,756
2002	622,711	554,994	134,508	39,592	69,165	330,981					19,252		67,717
2003	694,098	612,398	149,013	54,927	87,047	342,260					20,849		81,699
2004	750,785	660,668	151,324	68,031	94,432	365,611					18,729		90,117
2005	814,797	714,128	151,640	78,319	101,759	405,917					23,508		100,669
2006 ⁽¹⁾	891,000	773,530	156,592	88,321	114,214	444,849					30,446		117,470
2007 ⁽²⁾	982,737	849,026	163,213	77,377	121,090	521,471					34,125		133,711

Source: INSTAT.

1) Semifinal data.

2) Preliminary data.

1.7 EMPLOYMENT, UNEMPLOYMENT AND WAGES (In thousand, unless otherwise indicated)

	Labor force						Wages	
	Total employment					Unemployment Total registered unemployment	Average monthly wage in state sector (in Lek)	Minimum monthly wage approved (in Lek)
	In public sector	In agricultural private sector	In non agricultural private sector					
	1 = 2 + 6	2 = 3 + 4 + 5	3	4	5	6	7	8
2005	1,085	932	175	542	215	153	26,808	11,800
2006	1,084	935	169	542	224	150	28,822	14,000
2007 ¹⁾	1,383	1,198	167	569	230	185	33,750	16,100
2008 Q 1	1,080	939	167	542	231	141	35,800	16,000
Q 2	1,106	966	167	569	231	140	35,943	16,000
Q 3	1,110	970	167	569	235	140	36,093	17,000

Source: INSTAT.

1) Agricultural private sector data on employment are based on Labor Force Survey 2007.

2. GOVERNMENT FINANCE

2.1 GOVERNMENT BUDGET REVENUE (Progressive data in billion Lek, end of period)

	Total revenue						
		Grants	Tax revenue				Non tax revenue
			Revenue from tax offices and customs	Revenue from local government	Revenue from social contributions		
	1 = 2 + 3 + 7	2	3 = 4 + 5 + 6	4	5	6	7
2005	204,163	6,168	183,816	135,605	12,019	36,192	14,178
2006	229,444	8,025	205,523	155,102	11,112	39,309	15,895
2007	251,555	1,280	228,164	176,808	9,366	41,989	22,112
2008 ¹⁾ March	63,594	41	60,420	46,867	2,422	11,131	3,133
April	87,807	250	82,618	62,853	4,345	15,420	4,939
May	111,542	466	103,004	79,253	4,858	18,893	8,072
June	134,889	521	123,998	96,093	5,462	22,443	10,371
July	161,135	623	147,274	113,410	7,106	26,758	13,238
August	184,974	705	170,124	131,902	7,740	30,482	14,146
September	208,922	721	192,617	149,942	8,399	34,277	15,584
October	235,074	731	217,757	169,048	9,605	39,103	16,587
November	262,447	1,491	239,365	185,879	10,344	43,142	21,591

Source: Ministry of Finance

1) Preliminary data.

2.2 GOVERNMENT BUDGET EXPENDITURE (Progressive data, in billion Lek, end of period)

	Total expenditure												
	Current expenditure												Other expenditure
		Personnel expenditure	Interest	Operational & maintenance	Subsidies	Social insurance outlays	Local budget expenditure	Other current expenditure	Capital expenditure	Capital transfer			
	1=2+10+11+12	2=3+4+5+6+7+8+9	3	4	5	6	7	8	9	10	11	12	
2005	232,339	193,964	53,674	26,029	24,515	3,653	55,874	19,999	10,218	38,375		-	
2006	258,816	204,860	56,709	25,006	22,794	3,835	60,029	22,713	13,775	51,108	2,848	-	
2007	285,674	224,976	59,087	25,594	25,259	3,536	69,892	21,340	20,268	57,040	658	3,000	
2008 ¹⁾ March	53,098	48,032	14,172	6,926	3,703	207	16,640	3,776	2,608	5,066			
April	78,466	67,306	19,631	9,190	5,744	287	22,642	6,105	3,707	10,262		898	
May	105,621	87,291	24,700	12,359	7,856	700	28,623	8,222	4,831	16,984		1,346	
June	137,320	107,787	29,991	15,021	10,451	884	35,022	10,469	5,950	28,016		1,517	
July	166,722	129,752	35,646	18,758	12,804	961	41,796	12,723	7,062	34,744		2,227	
August	193,878	149,778	40,912	21,065	14,615	1,388	48,759	14,812	8,227	41,816		2,284	
September	217,317	169,539	46,344	22,994	16,624	1,506	55,423	17,196	9,452	45,450		2,328	
October	251,860	190,962	52,083	25,505	19,619	1,595	61,908	19,618	10,634	58,531		2,367	
November	284,341	212,829	58,034	28,599	22,182	1,791	68,130	22,338	11,756	69,135		2,376	

Source: Ministry of Finance

1) Preliminary data.

2.3 FISCAL DEFICIT AND ITS FINANCING (Progressive data, in billion Lek, end of period)

	Deficit financing										
	Budget deficit / surplus				Domestic financing				Foreign Financing		
	1	2 = 3 + 9	3=4+5+6+7+8	Treasury bills	Eurobonds	Loan	Bonds	Other liabilities	Long term loan	Change of statement accounts	
2005	-28,176	28,176	23,298	-4,047	0	0	0	27,345	5,857	-979	
2006	-29,372	29,372	23,623	-20,045	0	0	0	43,668	5,749	403	
2007	-34,119	34,119	28,829	-23,662	-5,549	0	46,250	11,790	5,289	279	
2008 ¹⁾ March	10,496	-10,496	-10,589	-4,420	0	0	9,870	-16,039	93	-178	
April	9,341	-9,341	-9,877	-4,220	0	-1,000	10,320	-14,977	536	35	
May	5,921	-5,921	-7,225	-6,257	0	-1,000	13,820	-13,787	1,303	38	
June	-2,431	2,431	-8,464	-7,178	0	-1,000	18,695	-18,981	10,896	145	
July	-5,588	5,588	-5,931	-8,178	0	-2,827	16,861	-11,787	11,519	139	
August	-8,904	8,904	-9,493	-8,230	0	-2,827	20,361	-18,797	18,396	609	
September	-8,395	8,395	-10,313	-8,202	0	-2,827	21,599	-20,881	18,708	506	
October	-16,786	16,786	-8,036	-11,087	0	-2,827	19,099	-13,221	24,822	627	
November	-21,894	21,894	-11,192	-13,239	0	-1,526	15,899	-12,326	33,086	773	

Source: Ministry of Finance

1) Preliminary data.

2.4 EXPENDITURE BY FUNCTIONS (COFOG) (Progressive data, in billion Lek, end of period)

	Total Expenditure											
		General public services ¹⁾	Defense	Public order and safety	Economic affairs	Environmental protection	Housing and community amenities	Health	Recreation, culture and religion	Education	Social protection	Other
	1 = 2 + 3 + 4 + 5 + 6 + 7 + 8 + 9 + 10 + 11 + 12	2	3	4	5	6	7	8	9	10	11	12
2007	285,674	54,385	11,494	15,171	51,833	88	12,671	24,104	3,219	31,630	77,421	3,658
2008 ²⁾ March	53,098	12,438	1,840	2,760	5,253	18	1,231	4,760	552	6,589	17,658	0
April	78,466	17,329	2,511	3,860	10,562	29	2,065	6,816	858	9,400	24,138	898
May	105,621	22,917	3,026	5,071	16,932	35	3,340	8,773	1,196	12,404	30,582	1,346
June	137,320	28,161	4,181	6,551	27,270	46	4,242	10,914	1,480	15,496	37,461	1,517
July	166,722	34,647	4,968	7,859	33,815	53	5,173	12,933	1,751	18,550	44,747	2,227
August	193,878	39,209	5,557	9,160	40,616	73	6,593	15,044	2,019	21,181	52,141	2,284
September	217,317	43,735	6,320	10,346	44,260	81	7,335	17,056	2,311	24,027	59,576	2,328
October	251,860	49,090	7,113	11,958	56,575	157	8,225	19,570	2,673	27,498	66,634	2,367
November	284,341	54,802	7,793	13,734	66,763	172	9,372	22,151	3,070	30,740	73,362	2,376

Source: Ministry of Finance

1) Comprise interest expenditure.

2) Preliminary data.

2.5. DOMESTIC DEBT¹⁾ (Progressive data, in billion Lek, end of period)

	Domestic debt stock								Other
	Treasury bills	2 years bonds	3 years bonds	5 years bonds	7 years bonds	Revaluation bonds of foreign currency with BoA			
	1 = 2 + 3 + 4 + 5 + 6 + 7 + 8	2	3	4	5	6	7	8	
2005	315,853	275,917	32,210	6,000	0	0	0	1,726	
2006	348,936	261,242	53,120	16,050	6,360	0	12,164	0	
2007	369,536	232,211	66,460	25,250	24,110	6,000	15,505	0	
2008 ¹⁾ Q1	374,986	227,791	70,130	25,950	29,610	6,000	15,505	0	
Q 2	390,212	225,032	71,430	25,100	33,110	12,000	23,540	0	
Q 3	390,888	224,008	71,630	23,100	36,610	12,000	23,540	0	

Source: Ministry of Finance

1) Preliminary data.

3. MONEY AND BANKING STATISTICS*

3.1 MONETARY AGGREGATES AND THEIR COMPONENTS

							M3
					M2	Deposits in foreign currency	
	M1			Time deposits in national currency			
	Currency in Circulation Outside Depository Corporations	Current accounts and demand deposits in national currency					
	1	2	3 (1+2)				4
	Outstanding at end of period (millions of Albanian Leke)						
2006 Dec.	163,264.3	79,126.4	242,390.7	234,982.1	477,372.8	189,094.6	666,467.4
2007 Dec.	154,956.2	87,719.3	242,675.5	263,461.7	506,137.2	251,472.3	757,609.5
2008 Jan.	146,947.6	78,772.8	225,720.4	276,133.0	501,853.4	257,028.2	758,881.6
Feb.	147,128.6	74,100.7	221,229.4	279,584.9	500,814.3	261,016.8	761,831.0
Mar.	146,812.6	68,392.9	215,205.5	283,044.0	498,249.6	256,264.3	754,513.9
Apr.	146,158.6	69,457.3	215,615.9	284,576.7	500,192.6	259,241.5	759,434.1
May	144,960.1	70,790.2	215,750.3	286,799.9	502,550.2	255,599.5	758,149.7
June	145,807.1	73,572.3	219,379.4	287,753.4	507,132.8	266,566.6	773,699.4
July	150,830.0	75,132.1	225,962.1	290,424.3	516,386.4	270,705.3	787,091.7
Aug.	152,262.4	74,552.3	226,814.6	293,897.7	520,712.3	287,620.1	808,332.4
Sep.	152,707.1	75,306.5	228,013.6	294,711.7	522,725.4	297,638.1	820,363.5
Oct.	165,297.3	74,413.5	239,710.8	284,651.3	524,362.0	282,284.0	806,646.0
Nov.	173,252.8	76,833.6	250,086.4	277,657.2	527,743.6	272,635.2	800,378.8
2008 Dec.	195,808.5	87,045.0	282,853.5	272,055.1	554,908.7	260,690.3	815,598.9
	Annual percentage changes						
2006 Dec.	9.08	6.95	8.38	15.88	11.95	29.03	16.32
2007 Dec.	(5.09)	10.86	0.12	12.12	6.03	32.99	13.68
2008 Jan.	(5.47)	4.52	(2.21)	13.19	5.71	32.19	13.40
Feb.	(4.79)	3.54	(2.16)	12.26	5.40	29.63	12.61
Mar.	(4.25)	(4.87)	(4.45)	12.77	4.63	26.64	11.19
Apr.	(4.39)	(2.08)	(3.66)	12.03	4.68	25.87	11.06
May	(4.45)	0.48	(2.89)	12.20	5.19	23.65	10.76
June	(2.86)	4.29	(0.58)	12.78	6.59	31.52	14.04
July	(0.69)	3.23	0.58	13.93	7.67	28.49	14.03
Aug.	1.15	5.95	2.68	14.36	8.96	21.84	13.22
Sep.	3.45	6.94	4.58	13.80	9.59	25.69	14.93
Oct.	15.08	5.41	11.90	8.59	10.08	17.47	12.56
Nov.	21.17	6.65	16.30	6.20	10.76	14.91	12.14
2008 Dec.	26.36	(0.77)	16.56	3.26	9.64	3.67	7.65

Source: Bank of Albania

* Preliminary data for December 2008

3.2 COUNTERPARTS OF MONETARY AGGREGATES

				Domestic assets	Other Items net
	Net foreign assets	Net claims on central government	Claims on other sectors*		
	1	2	3	4 (2+3)	
	Outstanding at end of period (millions of Albanian Leke)				
2006 Dec.	233,241.6	292,397.5	195,845.7	488,243.2	(7,680.0)
2007 Dec.	232,100.7	314,296.9	294,114.6	608,411.5	(6,748.9)
2008 Jan.	240,560.7	304,427.1	296,198.5	600,625.6	(7,733.7)
Feb.	236,109.0	304,648.3	309,236.0	613,884.3	(7,236.0)
Mar.	215,840.4	302,626.2	316,594.6	619,220.8	(7,262.4)
Apr.	208,975.9	303,714.5	326,559.0	630,273.5	(7,230.7)
May	196,229.0	307,793.4	334,634.3	642,427.7	(8,634.3)
June	198,188.0	307,766.6	348,496.5	656,263.1	(8,991.9)
July	200,505.3	311,077.0	357,271.5	668,348.5	(10,206.3)
Aug.	226,652.8	307,561.3	365,310.1	672,871.4	(8,034.1)
Sep.	236,477.1	306,874.7	378,017.6	684,892.3	(6,338.6)
Oct.	221,434.6	310,398.3	386,650.1	697,048.4	(6,294.5)
Nov.	225,486.8	292,525.3	395,632.1	688,157.4	(7,354.7)
2008 Dec.	206,667.7	322,065.6	396,569.2	718,634.8	(5,847.1)
	Annual percentage changes				
2006 Dec.	10.65	3.94	56.48	20.11	(14.60)
2007 Dec.	(0.49)	7.49	50.18	24.61	(12.12)
2008 Jan.	0.04	4.71	48.54	22.54	(4.06)
Feb.	(2.19)	4.08	48.11	22.41	87.05
Mar.	(8.09)	4.30	44.76	21.69	8.26
Apr.	(9.66)	5.30	43.88	22.29	(17.34)
May	(12.24)	6.73	43.29	23.09	(6.83)
June	(8.95)	7.88	45.10	24.89	35.49
July	(9.75)	8.93	45.59	25.87	26.63
Aug.	(7.95)	6.79	44.27	24.33	4.64
Sep.	(7.15)	12.79	44.85	28.48	36.03
Oct.	(10.54)	13.64	43.79	28.59	(4.43)
Nov.	(3.66)	5.48	42.75	24.11	10.99
2008 Dec.	(10.96)	2.47	34.83	18.12	(13.36)

Source: Bank of Albania

* "Claims on other sectors" include credit to economy and other claims on money holding sectors.

3.3 LEK DENOMINATED CURRENT ACCOUNTS AND DEMAND DEPOSITS BY SECTORS OF ECONOMY* (Millions of Albanian Leke)

	Total (1+2+3+4+5)					
	Local Government	Public Nonfinancial Corporations	Other Financial Corporations	Other Nonfinancial Corporations	Other Resident Sectors	
	1	2	3	4	5	6
2006 Dec.	685.1	9,024.0	630.9	17,647.8	51,138.6	79,126.4
2007 Dec.	478.7	11,459.8	557.2	31,871.7	43,351.8	87,719.3
2008 Jan.	474.9	7,604.5	812.8	27,585.9	42,294.7	78,772.8
Feb.	465.1	7,752.7	868.5	22,422.4	42,592.0	74,100.7
Mar.	481.5	8,552.8	739.5	15,705.6	42,913.5	68,392.9
Apr.	462.9	8,460.3	879.4	16,303.8	43,350.9	69,457.3
May	604.0	8,291.9	861.9	17,720.1	43,312.5	70,790.2
June	625.8	7,589.8	196.4	20,757.2	44,403.3	73,572.3
July	575.9	6,942.5	1,018.3	20,315.4	46,280.0	75,132.1
Aug.	591.3	7,452.4	1,097.0	21,506.1	43,905.4	74,552.3
Sep.	643.8	7,015.1	875.9	23,644.6	43,127.1	75,306.5
Oct.	478.3	6,818.6	1,043.4	25,281.4	40,791.8	74,413.5
Nov.	464.6	6,947.3	897.0	26,192.1	42,332.6	76,833.6
2008 Dec.	482.8	7,233.9	698.2	33,582.0	45,048.2	87,045.0

Source: Bank of Albania

*Deposits included in broad money

3.4 LEK DENOMINATED TIME DEPOSITS BY SECTORS OF ECONOMY* (Millions of Albanian Leke)

	Total (1+2+3+4+5)					
	Local Government	Public Nonfinancial Corporations	Other Financial Corporations	Other Nonfinancial Corporations	Other Resident Sectors	
	1	2	3	4	5	6
2006 Dec.	1.1	1,603.7	276.4	8,376.0	224,724.9	234,982.1
2007 Dec.	206.4	2,476.6	300.4	5,777.0	254,701.3	263,461.7
2008 Jan.	221.2	3,241.8	673.3	5,887.8	266,108.9	276,133.0
Feb.	174.1	2,791.8	270.3	6,718.6	269,630.2	279,584.9
Mar.	113.1	2,843.6	306.0	7,533.5	272,247.8	283,044.0
Apr.	1.1	3,329.8	333.7	7,512.5	273,399.6	284,576.7
May	1.1	2,819.5	505.0	8,160.0	275,314.2	286,799.9
June	1.1	2,846.0	505.9	8,644.9	275,755.4	287,753.4
July	15.1	2,763.5	1,534.9	9,678.8	276,431.9	290,424.3
Aug.	18.0	2,797.5	756.6	10,274.8	280,050.8	293,897.7
Sep.	12.2	2,863.1	468.3	6,648.4	284,719.7	294,711.7
Oct.	12.3	1,590.6	1,501.7	7,449.1	274,097.5	284,651.3
Nov.	12.4	1,176.0	1,079.8	7,939.5	267,449.6	277,657.2
2008 Dec.	17.7	1,331.5	831.8	9,428.6	260,445.6	272,055.1

Source: Bank of Albania

*Deposits included in broad money

3.5 FOREIGN CURRENCY DENOMINATED CURRENT ACCOUNTS AND DEMAND DEPOSITS BY SECTORS OF ECONOMY* (Millions of Albanian Leke)

	Total (1+2+3+4+5)					
	Local Government	Public Nonfinancial Corporations	Other Financial Corporations	Other Nonfinancial Corporations	Other Resident Sectors	
	1	2	3	4	5	6
2006 Dec.	1,438.4	4,268.9	200.2	18,289.8	38,146.7	62,344.0
2007 Dec.	221.8	3,440.4	299.0	23,003.6	42,497.6	69,462.3
2008 Jan.	158.5	3,214.2	137.1	22,264.0	42,048.8	67,822.5
Feb.	207.3	2,217.9	149.4	20,896.9	42,934.3	66,405.8
Mar.	177.9	2,318.7	278.9	22,426.1	40,963.0	66,164.7
Apr.	160.2	2,787.3	313.2	22,751.8	41,148.2	67,160.7
May	139.8	2,299.9	203.5	22,444.2	41,928.7	67,016.1
June	142.6	2,531.3	317.6	27,708.0	42,613.1	73,312.7
July	81.4	2,825.2	173.6	26,350.0	43,750.6	73,180.7
Aug.	99.4	2,212.7	195.0	28,707.5	45,471.1	76,685.6
Sep.	158.7	2,566.3	296.4	29,033.8	45,098.6	77,153.8
Oct.	150.7	3,464.6	224.2	27,219.6	40,403.0	71,462.2
Nov.	153.5	3,215.0	445.7	24,308.1	39,675.9	67,798.1
2008 Dec.	108.8	2,609.4	608.7	23,225.7	38,561.2	65,113.8

Source: Bank of Albania

*Deposits included in broad money.

3.6 FOREIGN CURRENCY DENOMINATED TIME DEPOSITS BY SECTORS OF ECONOMY* (Millions of Albanian Leke)

	Total (1 + 2 + 3 + 4 + 5)					
	Local Government	Public Nonfinancial Corporations	Other Financial Corporations	Other Nonfinancial Corporations	Other Resident Sectors	
	1	2	3	4	5	6
2006 Dec.	70.7	2,891.3	794.1	16,715.2	106,279.4	126,750.6
2007 Dec.	149.7	4,523.3	1,270.4	22,787.9	153,278.8	182,010.0
2008 Jan.	150.7	4,485.3	872.7	23,222.4	160,474.6	189,205.7
Feb.	170.5	4,605.1	1,048.6	23,208.5	165,578.3	194,611.0
Mar.	168.3	5,287.3	624.1	21,681.0	162,339.0	190,099.7
Apr.	167.0	5,281.6	574.9	21,179.7	164,877.5	192,080.7
May	609.3	5,418.5	1,385.0	13,465.0	167,705.6	188,583.5
June	602.5	5,280.8	1,578.3	17,006.0	168,786.4	193,253.9
July	748.7	5,189.3	1,398.3	17,653.1	172,535.1	197,524.5
Aug.	781.1	5,343.7	1,526.1	17,933.8	185,349.7	210,934.5
Sep.	811.8	6,069.1	1,445.5	16,528.6	195,629.3	220,484.3
Oct.	882.3	5,337.1	1,752.0	20,290.0	182,560.4	210,821.8
Nov.	262.4	5,877.1	1,443.1	22,513.8	174,740.7	204,837.1
2008 Dec.	170.7	5,480.3	1,731.1	22,697.2	165,497.2	195,576.5

Source: Bank of Albania

*Deposits included in broad money.

3.7 CREDIT TO ECONOMY BY SECTORS (Millions of Albanian Leke)

	Loans in national currency												Loans in foreign currency				Total				
	Local Government						Public Nonfinancial Corporations						Other Financial Corporations					Other Nonfinancial Corporations		Other Resident Sectors	
	1	2	3	4	5	6 (1+2+3+4+5)	7	8	9	10	11	12 (7+8 +9+10+11)	13 (6+12)								
2006 Dec.	-	2.1	-	26,285.5	32,868.9	59,156.5	-	173.5	58.1	100,799.3	35,559.4	136,590.3	195,746.8								
2007 Dec.	-	0.0	70.2	35,708.3	49,057.9	84,836.4	-	3,923.0	27.2	146,340.7	58,736.4	209,027.3	293,863.7								
2008 Jan.	-	0.1	120.8	35,585.7	49,583.6	85,290.2	-	4,152.2	16.9	145,953.1	60,535.3	210,657.5	295,947.7								
Feb.	-	1.5	185.2	36,107.2	50,207.5	86,501.5	-	4,323.7	21.2	153,767.4	64,370.7	222,483.1	308,984.6								
Mar.	-	1.7	185.6	37,694.3	51,132.7	89,014.3	-	4,448.4	3.2	157,710.6	65,114.6	227,276.8	316,291.1								
Apr.	-	1.6	230.1	38,999.7	52,275.6	91,507.0	-	5,973.1	122.8	161,084.4	67,567.9	234,748.1	326,255.2								
May	-	1.6	186.5	40,406.9	53,809.1	94,404.1	-	6,024.6	-	164,664.5	69,233.6	239,922.7	334,326.7								
June	-	1.6	185.8	42,934.4	55,293.9	98,415.7	-	4,555.3	-	173,466.5	71,816.8	249,838.6	348,254.3								
July	-	3.1	185.1	42,361.2	56,415.6	98,965.0	-	6,014.9	-	178,984.0	73,067.9	258,066.8	357,031.8								
Aug.	-	898.8	186.6	43,148.1	57,276.8	101,510.3	-	6,038.1	60.9	182,759.2	74,701.2	263,559.4	365,069.7								
Sep.	-	1,092.3	185.7	45,047.6	58,141.2	104,466.8	-	6,112.9	56.9	189,454.1	77,585.9	273,209.8	377,676.6								
Oct.	-	1,615.1	232.3	46,148.7	59,914.2	107,910.3	-	6,091.4	51.6	192,968.9	79,286.4	278,398.2	386,308.5								
Nov.	-	2,828.7	334.0	47,566.9	60,530.6	111,260.3	-	6,043.4	46.5	198,262.2	79,677.9	284,030.0	395,290.2								
2008 Dec.	-	3,636.7	334.7	49,111.0	60,936.2	114,018.6	-	9,262.4	41.5	192,939.7	79,968.9	282,212.4	396,231.0								

Source: Bank of Albania

3.8 SECTORIAL BALANCE SHEET OF DEPOSIT MONEY BANKS (Millions of Albanian Leke)

	Total assets (1+2+6+9+18+21+16+22+23)																															
	National currency		Foreign currency		Deposits (3+4+5)				Securities other than shares (7+8)				Loans (10+11+12+13+14+15+16+17)								Shares and other capital (19+20)				Other receivable accounts		Nonfinancial assets					
	1	2	Nonresidents		Bank of Albania		Deposit Money Banks		Central Government		Nonresidents		Bank of Albania		Deposit Money Banks		Other Financial Corporations		Central Government		Public Nonfinancial Corporations		Other Nonfinancial Corporations		Other Resident Sectors		Nonresidents	Residents	21	22	23	24
2006 Dec.	4,983.3	8,777.2	82,927.2	55,312.5	3,073.0	141,312.7	10,628.8	241,756.0	252,384.8	5,439.6	4,200.9	430.2	58.1	0.0	175.6	127,084.8	64,965.4	202,354.6	2,144.3	97.5	2,241.8	2,712.7	8,851.0	623,618.0								
2007 Dec.	6,214.6	9,698.0	83,653.3	66,426.5	2,388.0	152,467.7	7,451.5	254,729.9	262,181.5	2,923.6	-	200.1	97.4	-	3,923.0	182,049.1	103,376.0	292,569.1	1,499.2	96.9	1,596.1	2,978.9	11,230.7	738,936.7								
2008 Jan.	6,486.0	7,993.1	87,921.9	63,750.1	2,344.9	154,016.9	7,285.9	254,061.7	261,347.6	2,930.8	8,530.6	331.2	137.7	-	4,152.3	181,538.8	105,663.1	303,284.4	1,502.0	96.9	1,598.9	3,026.6	11,288.8	749,042.5								
Feb.	5,704.5	8,034.9	93,848.2	64,855.8	3,505.8	162,209.9	7,313.3	257,243.0	264,556.3	2,535.1	4,515.2	454.7	206.5	-	4,325.2	189,874.7	110,124.2	312,035.5	1,508.5	96.9	1,605.4	3,132.4	11,517.8	768,796.6								
Mar.	7,239.6	7,164.0	90,601.5	60,863.8	4,430.7	155,895.9	5,646.4	260,095.9	265,742.3	1,612.9	3,099.3	55.0	188.7	-	4,450.2	195,404.9	111,579.3	316,390.3	1,448.6	96.7	1,545.3	3,756.8	11,747.5	769,481.7								
Apr.	6,410.6	8,213.6	86,823.2	3,255.1	153,755.5	5,788.2	260,785.3	266,573.5	1,805.0	2,207.5	678.8	352.8	-	-	5,974.6	200,084.1	115,148.7	324,251.6	1,189.2	106.9	1,296.1	4,020.4	12,112.2	778,633.6								
May	6,118.4	6,985.3	81,626.5	63,743.3	4,897.5	150,267.3	5,669.6	261,542.5	267,212.1	1,722.8	795.0	225.0	186.5	-	6,026.2	205,071.4	118,341.0	332,368.0	1,366.5	106.8	1,473.4	3,571.7	12,965.9	780,962.0								
June	7,356.3	8,022.5	82,759.7	67,437.6	4,329.1	154,526.3	5,518.5	266,388.8	271,907.3	1,715.6	-	510.1	185.8	1,831.1	4,556.9	216,401.0	122,207.2	347,407.6	1,336.9	96.6	1,433.5	3,659.4	13,160.5	807,473.4								
July	6,263.8	8,625.9	86,456.5	69,367.6	5,731.3	161,555.8	5,556.4	263,048.5	268,604.9	1,660.1	-	540.0	185.1	1,836.7	6,018.0	221,345.2	124,585.0	356,170.0	1,295.6	96.6	1,392.2	3,583.7	13,740.2	819,936.1								
Aug.	7,640.0	9,531.8	97,496.5	66,362.5	6,799.8	170,658.8	5,802.7	267,179.8	272,982.5	1,907.6	-	585.1	247.5	1,844.5	6,936.9	225,907.4	127,074.4	364,503.3	1,259.5	96.9	1,356.4	3,716.9	13,955.0	844,364.7								
Sep.	7,397.5	8,256.0	95,554.3	67,049.1	6,698.4	169,301.8	7,299.7	267,569.1	274,868.8	3,207.1	-	160.0	242.6	1,866.8	7,205.2	234,501.7	130,735.7	377,919.1	2,012.2	97.1	2,109.3	3,919.3	14,133.8	857,905.5								
Oct.	7,034.9	11,253.3	76,432.0	69,840.4	5,490.3	151,762.6	9,484.4	263,995.0	273,479.4	3,399.9	-	25.0	283.9	1,867.6	7,706.5	239,117.6	134,198.4	386,598.8	2,030.0	97.7	2,127.7	4,047.4	14,620.5	850,924.6								
Nov.	7,661.5	9,381.7	64,185.4	66,175.9	4,077.7	134,439.1	13,482.1	254,913.0	268,395.1	3,792.5	-	55.0	380.5	1,877.6	8,872.2	245,829.0	135,196.7	396,003.6	1,997.7	97.6	2,095.3	4,310.7	14,892.2	837,179.2								
2008 Dec.	7,901.2	11,621.6	55,812.2	68,645.1	2,097.5	126,554.8	13,533.1	259,034.3	272,567.3	3,642.5	-	280.2	376.2	1,868.9	12,899.1	242,050.6	135,873.0	396,990.4	1,977.1	97.2	2,074.3	4,040.0	15,248.6	836,998.2								

	Deposits included in broad money (1+2+3+4+5)										Deposits excluded from broad money (7+8+9+10+11+12+13+14)										Loans (17+18+19+20+21+22)							Total liabilities and capital (6+15+16+23+24+25)																																
	Local Government					Public Nonfinancial Corporations					Other Nonfinancial Corporations					Other Resident Sectors					Nonresidents					Bank of Albania					Other Depository Corporations					Central Government					Other Financial Corporations					Other Nonfinancial Corporations					Other accounts payable					Shares and other equity				
	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	16	17	18	19	20	21	22	23	24	25	26																																		
2006 Dec.	1,899.7	2,195.2	17,787.9	61,028.8	419,685.0	502,596.7	23,601.7	1,135.3	2,253.7	1,162.5	-	122.7	8,277.7	7,539.9	44,093.7	-	14,395.4	9,046.1	1,119.0	206.6	-	530.1	25,297.1	6,732.3	44,898.3	623,618.0																																		
2007 Dec.	2,411.3	1,056.6	21,900.1	83,440.2	492,833.4	601,641.6	14,780.9	66.4	2,847.8	1,669.9	0.4	262.8	8,544.5	9,784.2	37,956.9	-	29,371.0	1,605.2	608.9	131.1	243.6	492.2	32,452.0	7,191.8	59,694.4	738,936.7																																		
2008 Jan.	2,101.0	1,005.3	18,545.8	78,960.0	509,931.6	610,543.8	8,346.6	339.4	3,595.4	2,551.6	0.4	268.1	7,525.9	10,480.3	33,107.8	-	29,341.4	97.2	782.6	129.7	246.5	496.5	31,093.9	10,962.6	63,334.4	749,042.5																																		
Feb.	2,334.6	1,016.9	17,367.6	73,246.4	519,738.0	613,703.5	9,094.0	133.1	3,399.3	2,563.5	4.0	290.9	7,677.9	10,377.2	33,539.9	-	42,013.0	99.8	1,814.7	131.4	-	504.4	44,563.1	12,241.4	64,748.7	768,796.6																																		
Mar.	1,946.1	940.8	19,002.4	67,346.1	517,351.0	606,586.4	10,511.1	1,583.1	3,982.6	2,465.8	0.3	291.7	6,645.0	10,180.2	35,659.8	-	46,757.1	1,833.2	1,919.8	131.3	371.6	119.9	51,132.8	13,477.9	62,624.8	769,481.7																																		
Apr.	2,049.7	791.2	19,859.0	67,747.7	521,663.4	612,110.9	11,186.0	463.0	4,749.2	2,277.0	0.3	80.9	7,316.4	9,745.6	35,818.4	-	48,324.6	4,424.8	1,214.3	131.5	370.7	121.7	54,587.6	12,788.2	63,328.5	778,633.6																																		
May	2,955.0	1,354.2	18,829.8	61,789.2	527,148.9	612,077.1	9,243.7	774.9	2,970.1	1,924.0	0.3	72.3	7,214.1	9,882.3	32,001.8	-	53,299.7	955.1	3,191.4	131.4	370.3	122.2	58,070.1	12,813.4	65,999.7	780,962.1																																		
June	2,597.6	1,372.1	18,247.9	74,116.1	530,409.0	626,742.7	7,932.8	1,327.5	3,890.6	1,659.0	0.4	74.6	6,984.2	9,876.1	31,825.1	-	58,551.7	7,796.3	2,345.4	82.1	372.3	115.8	69,263.6	12,607.7	67,034.3	807,473.4																																		
July	3,878.2	1,421.1	17,720.6	73,977.3	537,847.4	634,864.5	11,565.6	939.4	3,383.8	2,043.0	0.4	72.3	6,786.5	9,941.3	34,732.4	-	61,633.8	3,811.3	4,168.8	56.3	367.4	101.4	70,139.1	11,660.0	68,540.1	819,936.1																																		
Aug.	3,558.1	1,489.9	17,806.3	78,422.2	553,627.0	654,903.5	11,388.3	371.4	3,969.0	3,090.2	0.4	68.8	7,163.2	11,046.6	37,097.9	-	58,715.0	3,638.9	4,659.7	56.8	368.1	-	67,438.5	14,544.3	70,380.6	844,364.7																																		
Sep.	3,074.9	1,626.5	18,513.6	75,855.5	567,345.1	666,415.6	11,706.8	364.3	3,462.2	2,601.9	0.4	70.9	7,238.9	11,382.5	36,828.0	-	56,676.7	4,020.5	4,618.3	57.7	379.0	-	65,752.1	17,133.4	71,776.5	857,905.5																																		
Oct.	3,788.4	1,523.7	17,210.9	80,240.1	536,623.5	639,397.8	14,505.0	1,289.6	1,955.2	2,290.5	0.4	77.1	7,056.9	11,460.5	38,635.3	-	62,501.5	15,395.1	4,998.8	58.0	378.0	-	83,322.3	16,640.2	72,940.3	850,924.6																																		
Nov.	3,367.3	892.9	17,215.4	80,953.5	522,968.7	625,397.8	14,197.7	719.1	903.6	1,965.6	0.4	79.8	6,744.7	11,386.4	35,997.3	-	65,662.9	14,412.6	3,980.8	58.5	380.2	-	84,495.0	16,798.9	74,490.1	837,179.2																																		
2008 Dec.	3,664.2	780.0	16,655.0	88,933.6	508,323.9	618,356.6	13,422.0	505.3	1,405.8	2,271.7	0.4	77.3	6,395.6	11,637.3	35,715.5	-	68,092.5	20,145.3	1,741.3	58.6	383.5	-	90,421.2	17,996.1	74,508.9	836,998.2																																		

Source: Bank of Albania

3.9 SECTORIAL BALANCE SHEET OF BANK OF ALBANIA (Millions of Albanian Leke)

	Total assets (1+2+3+6+10+11+12)											
	Holdings of SDRs			Foreign currency			Deposits			Securities other than shares (4+5)		
	1	2	3	4	5	6	Nonresidents	Central Government	Other Depository Corporations	Other Resident Sectors	Loans (7+8+9)	Other receivable accounts
2006 Dec.	855.3	16.9	42,297.2	127,039.7	67,940.8	194,980.5	-	-	9,042.5	871.4	9,913.9	12,547.6
2007 Dec.	163.3	5.1	45,773.8	132,843.0	72,892.2	205,735.1	-	-	1,603.5	1,047.9	2,651.4	13,406.0
2008 Jan.	1,065.3	5.7	51,084.1	126,427.9	72,686.7	199,114.6	-	-	95.4	1,085.4	1,180.8	7,941.0
Feb.	927.1	6.1	47,762.8	132,787.1	64,859.9	197,647.0	-	-	97.5	1,083.6	1,181.1	8,705.7
Mar.	903.9	5.1	52,176.2	120,965.1	64,418.0	185,383.1	-	-	1,832.6	1,081.3	2,914.0	8,143.9
Apr.	1,215.2	15.7	52,746.4	118,255.8	64,342.0	182,597.7	-	-	4,423.4	1,108.1	5,531.6	8,922.2
May	1,130.7	11.0	45,686.6	122,273.3	64,415.1	186,688.4	-	-	953.9	1,114.9	2,068.8	9,758.0
June	900.6	7.2	45,097.1	126,506.4	64,484.3	190,990.7	-	-	7,793.8	1,128.6	8,922.4	9,982.0
July	851.0	7.4	55,312.0	120,783.2	64,125.4	184,908.5	-	-	3,809.1	1,123.8	4,932.9	10,150.1
Aug.	890.0	7.1	63,286.7	123,718.2	64,303.4	188,021.6	-	-	3,635.2	1,128.8	4,764.0	10,108.7
Sep.	877.6	16.0	62,304.3	133,124.7	64,437.5	197,562.3	-	-	4,018.7	1,136.8	5,155.4	10,041.8
Oct.	943.1	1,113.8	53,835.9	147,705.6	64,392.3	212,097.9	-	-	15,391.8	1,147.6	16,539.4	10,346.6
Nov.	914.7	1,103.3	62,935.9	155,103.3	67,351.7	222,455.0	-	-	14,404.6	1,157.2	15,561.8	13,492.1
2008 Dec.	641.8	1,068.6	64,087.6	142,952.5	75,167.2	218,119.8	3,000.0	-	20,141.0	1,177.6	24,318.6	12,891.3
Total liabilities and capital (1+2+8+12+13+14)												
	Currency in circulation			Deposits included in broad money (2+3)			Deposits excluded from broad money (3+4+5+6+7)					
	1	2	3	4	5	6	7	8	9	10	11	12
	Nonresidents	Central Government	Other Depository Corporations	Other Nonfinancial Corporations	Other Resident Sectors	Other Resident Sectors	Nonresidents	Central Government	Other Depository Corporations	Other accounts payable	Shares and other equity	13
2006 Dec.	168,254.9	2.8	6,922.6	21,106.8	49,367.0	6.2	636.4	78,038.9	1,241.3	4,200.3	-	5,441.6
2007 Dec.	161,181.9	13.4	7,150.5	20,775.7	67,035.6	8.2	586.7	95,556.8	1,186.4	-	-	1,186.4
2008 Jan.	153,444.8	391.8	7,152.1	18,691.9	63,383.7	8.3	523.5	89,759.6	1,194.2	8,529.2	-	9,723.4
Feb.	152,844.2	0.5	7,152.1	14,041.2	64,849.7	7.4	476.5	86,526.8	1,211.4	4,514.5	-	5,725.8
Mar.	154,070.3	0.1	7,151.1	17,914.1	59,507.3	7.9	456.9	85,037.4	1,182.9	3,098.9	-	4,281.8
Apr.	152,587.3	49.7	7,323.8	18,504.7	63,329.5	8.1	366.0	89,532.2	1,177.0	2,207.3	-	3,384.3
May	151,096.5	(2.2)	6,625.5	17,165.1	63,276.1	7.8	438.0	87,512.4	1,168.6	794.9	-	1,963.4
June	153,177.6	(2.0)	6,625.1	24,160.7	66,563.0	12.5	473.1	97,834.4	1,172.4	-	-	1,172.4
July	157,107.9	245.6	6,781.4	16,917.0	68,561.7	12.8	342.4	92,615.2	1,173.7	-	-	1,173.7
Aug.	159,936.5	15.1	6,782.5	23,223.2	66,470.6	12.9	417.4	96,906.5	1,165.8	-	-	1,165.8
Sep.	160,127.7	10.0	6,783.3	25,100.9	66,732.5	12.3	541.1	99,170.1	1,176.7	-	-	1,176.7
Oct.	172,355.3	731.4	6,785.7	18,804.1	68,867.8	12.2	764.2	95,233.9	1,171.7	-	-	1,171.7
Nov.	180,937.4	497.4	6,785.4	34,057.3	65,808.1	12.2	716.7	107,379.6	1,168.4	-	-	1,168.4
2008 Dec.	203,732.8	203.1	6,783.7	19,334.8	67,793.3	12.2	890.7	94,814.7	1,173.4	-	-	1,173.4

Source: Bank of Albania

4. FINANCIAL MARKETS*

4.1 CURRENCY BREAKDOWN OF INTEREST RATE ON NEW LOANS** (In percentage)

	Interest rates on loans in Leke				
	Up to 6 months	6 months - 1 year	1-3 years	3 - 5 years	Over 5 years
2006 Dec.	12.18	11.16	17.61	14.60	10.86
2007 Dec.	13.85	13.55	14.55	14.64	13.72
2008 Jan.	15.53	13.36	16.26	15.04	14.01
Feb.	14.29	11.78	14.30	15.04	13.44
Mar.	13.50	11.48	15.02	14.78	13.18
Apr.	12.40	12.92	16.00	14.58	13.13
May	12.40	11.50	16.10	14.90	12.30
June	13.66	11.04	15.72	13.88	11.55
July	12.49	11.45	15.13	14.07	11.63
Aug.	12.04	12.32	15.78	14.44	11.60
Sep.	12.30	10.80	15.70	14.10	13.30
Oct.	12.99	12.46	15.60	14.17	12.21
Nov.	13.44	12.05	14.39	13.90	12.13
2008 Dec.	11.18	10.76	12.69	12.78	13.20
	Interest rates on loans in USD				
	Up to 6 months	6 months - 1 year	1-3 years	3 - 5 years	Over 5 years
2006 Dec.	9.76	9.11	10.00	9.74	8.86
2007 Dec.	8.78	8.46	7.79	8.81	8.91
2008 Jan.	8.35	9.42	7.39	-	16.23
Feb.	7.96	6.79	5.15	-	8.69
Mar.	6.51	7.01	7.47	6.21	6.51
Apr.	7.63	7.00	6.94	6.81	6.74
May	7.40	6.70	6.80	6.20	7.10
June	7.17	6.87	7.16	8.94	7.00
July	6.89	6.48	6.88	7.27	7.01
Aug.	6.94	7.36	7.01	9.03	6.78
Sep.	8.96	7.38	9.11	8.74	5.71
Oct.	7.88	7.51	6.90	7.49	5.58
Nov.	7.53	8.11	8.49	9.35	6.81
2008 Dec.	6.84	6.98	6.96	7.29	6.02
	Interest rates on loans in Euro				
	Up to 6 months	6 months - 1 year	1-3 years	3 - 5 years	Over 5 years
2006 Dec.	29.67	18.29	11.30	16.22	36.52
2007 Dec.	8.73	8.88	9.30	9.23	8.26
2008 Jan.	9.40	8.12	7.86	9.14	8.10
Feb.	8.20	7.07	6.19	9.14	7.73
Mar.	8.39	7.50	8.36	7.94	7.55
Apr.	8.96	8.39	9.17	8.61	8.16
May	8.50	8.70	9.70	8.70	8.00
June	9.06	8.62	9.69	9.51	7.97
July	8.53	7.98	9.52	7.61	8.39
Aug.	8.24	8.59	8.77	9.59	7.75
Sep.	8.80	9.35	9.42	9.12	7.76
Oct.	8.74	8.50	9.30	9.42	8.00
Nov.	8.89	8.41	8.06	7.86	7.24
2008 Dec.	8.18	6.72	7.89	6.83	7.42

Source: Bank of Albania

* Preliminary data for December 2008

**Weighted average interest rates

4.2 CURRENCY BREAKDOWN OF INTEREST RATE ON NEW DEPOSITS* (In percentage)

	Interest rates in Leke								
	60 months	48 months	36 months	24 months	12 months	6 months	3 months	1 months	Current accounts
2006 Dec.	-	-	6.42	5.88	5.46	4.64	3.94	3.35	0.20
2007 Dec.	8.00	-	7.30	6.59	6.33	5.50	4.85	3.21	0.11
2008 Jan.	7.75	-	7.76	6.87	6.49	5.65	5.08	3.59	0.11
Feb.	7.75	-	7.48	6.69	6.10	5.44	4.80	3.48	0.46
Mar.	6.06	-	7.44	6.56	6.11	5.42	4.84	3.58	0.45
Apr.	6.94	-	7.03	6.69	6.41	5.64	5.06	3.62	0.46
May	7.50	7.30	7.05	6.62	6.72	5.61	4.96	4.36	0.43
June	6.90	-	7.34	6.74	6.55	5.76	5.00	4.61	0.34
July	8.06	-	7.49	7.37	7.72	5.99	5.21	4.63	0.36
Aug.	8.49	-	7.57	7.18	7.71	6.09	6.27	5.09	0.29
Sep.	8.61	-	7.41	6.83	7.25	5.81	5.08	4.89	0.27
Oct.	9.41	-	7.27	6.88	6.90	5.76	5.02	4.84	0.25
Nov.	7.80	-	7.18	6.92	6.82	5.95	5.09	4.73	0.27
2008 Dec.	7.51	-	7.49	6.83	6.86	5.76	5.23	3.95	0.26
	Interest rates in USD								
	60 months	48 months	36 months	24 months	12 months	6 months	3 months	1 months	Current accounts
2006 Dec.	5.30	-	5.03	4.86	4.29	3.87	3.44	3.03	0.21
2007 Dec.	5.20	-	5.04	4.43	4.10	3.63	3.37	3.59	0.11
2008 Jan.	5.20	-	5.07	4.47	4.03	3.45	3.25	2.74	0.13
Feb.	3.80	3.30	4.08	4.11	3.47	3.95	2.90	2.94	0.18
Mar.	3.80	-	2.86	4.08	3.03	2.94	2.52	2.43	0.17
Apr.	-	-	3.61	3.86	2.69	2.45	2.29	2.24	0.18
May	3.70	3.00	2.51	2.98	2.61	2.40	2.42	2.13	0.18
June	3.80	-	2.23	2.98	2.78	2.40	2.30	2.21	0.15
July	3.13	-	2.54	2.61	3.04	2.24	2.24	2.48	0.15
Aug.	3.94	-	2.45	2.74	3.68	2.31	2.28	2.16	0.13
Sep.	3.77	-	2.57	3.04	2.93	2.36	2.21	2.13	0.13
Oct.	4.00	-	2.41	2.73	2.48	2.17	1.97	2.05	0.14
Nov.	3.70	-	2.28	2.84	2.70	2.10	2.10	2.14	0.14
2008 Dec.	-	-	1.80	2.44	2.55	2.20	2.07	1.76	0.14
	Interest rates in EURO								
	60 months	48 months	36 months	24 months	12 months	6 months	3 months	1 months	Current accounts
2006 Dec.	4.73	-	4.31	4.16	3.45	3.29	2.91	2.54	0.10
2007 Dec.	5.61	-	4.51	4.44	4.23	3.92	3.59	2.69	0.11
2008 Jan.	5.90	-	4.46	4.36	4.19	3.81	3.68	2.65	0.10
Feb.	5.99	5.21	4.99	4.41	4.22	3.84	3.71	2.90	0.21
Mar.	5.65	-	4.50	4.57	4.12	3.77	3.83	3.55	0.83
Apr.	5.74	-	4.39	4.76	4.53	4.22	3.80	4.18	0.22
May	5.73	4.85	4.34	4.41	4.78	3.90	3.76	3.94	0.20
June	4.92	-	5.31	4.82	4.74	3.98	3.82	3.99	0.17
July	6.00	-	4.74	4.91	5.36	4.33	3.95	4.08	0.20
Aug.	5.83	5.00	5.08	4.91	5.51	4.40	4.23	3.88	0.16
Sep.	6.35	5.00	5.93	4.94	4.85	4.52	4.14	3.88	0.16
Oct.	5.56	5.00	4.53	4.50	4.94	4.37	4.00	3.89	0.16
Nov.	4.71	-	4.70	5.16	4.83	4.45	3.97	3.93	0.15
2008 Dec.	4.71	-	4.80	4.71	4.70	4.24	4.13	2.94	0.15

Source: Bank of Albania

*Weighted average interest rate

4.3 TREASURY BILLS YIELDS* (In percentage)

	Maturity breakdown of Treasury bill yields		
	3-month	6-month	12-month
2007 Jan.	6.32	7.18	7.87
Feb.	6.17	7.07	7.72
Mar.	5.76	6.70	7.16
Apr.	5.76	6.98	7.67
May	5.75	7.20	7.99
June	5.68	7.21	7.96
July	5.81	7.26	7.99
Aug.	5.78	7.25	7.97
Sep.	5.74	7.27	7.99
Oct.	6.06	7.38	8.10
Nov.	6.04	7.35	8.07
2007 Dec.	6.32	7.41	8.26
2008 Jan.	6.27	7.36	8.23
Feb.	6.26	7.29	8.00
Mar.	6.25	7.36	8.02
Apr.	6.29	7.41	8.12
May	6.28	7.48	8.16
June	6.27	7.46	8.20
July	6.28	7.46	8.21
Aug.	6.26	7.39	8.15
Sep.	6.25	7.33	8.02
Oct.	6.23	7.20	7.94
Nov.	6.05	7.42	8.10
2008 Dec.	6.19	7.45	8.56

Source: Bank of Albania

*Weighted average interest rates

5. EXCHANGE RATE

5.1 THE LEK OFFICIAL EXCHANGE RATE VERSUS FOREIGN CURRENCIES (Leks per unit of foreign currencies)

Main foreign currencies	Period weighted average				End of period			
	US Dollar (USD)	European currency (EUR)	British pound sterling (GBP)	Swiss Franc (CHF)	US Dollar (USD)	European currency (EUR)	British pound sterling (GBP)	Swiss Franc (CHF)
	1	2	3	4	5	6	7	8
2004	102.78	127.67	188.22	82.70	92.64	126.35	178.69	81.87
2005	99.87	124.19	181.58	80.23	103.58	122.58	178.65	78.86
2006	98.10	123.08	180.56	78.29	94.14	123.85	184.65	77.17
2007	90.43	123.62	180.83	75.31	82.89	121.78	166.02	73.65
2008 Jan.	83.39	122.61	164.14	75.77	82.61	122.61	164.37	76.35
Feb.	83.89	123.69	164.75	76.92	82.58	125.34	163.67	78.74
Mar.	80.32	124.59	160.75	79.41	78.29	123.70	155.39	78.87
Apr.	77.79	122.68	154.05	76.93	78.94	122.75	155.41	76.08
May	78.45	122.08	154.15	75.18	78.65	122.01	155.19	74.90
Jun.	78.46	122.03	154.04	75.59	77.17	122.05	153.93	76.02
Jul.	77.24	121.87	153.58	75.29	78.01	121.80	154.66	74.54
Aug.	81.12	121.44	153.21	74.92	82.66	121.70	151.25	75.32
Sep.	85.65	123.05	153.95	77.16	86.38	123.89	155.56	78.04
Oct.	92.62	123.13	156.14	81.14	96.78	123.30	156.22	84.08
Nov.	96.84	123.29	148.68	81.48	95.33	123.37	147.46	79.65
Dec.	90.96	123.18	135.05	80.17	87.91	123.80	127.66	82.97

Source: Bank of Albania

6. INTEREST RATES OF MONETARY POLICY INSTRUMENTS

6.1 BANK OF ALBANIA KEY INTEREST RATES (In percentage)

		Overnight deposit		Weekly repurchase agreement		Overnight credit		Lombard credit	
		Level	Change	Level	Change	Level	Change	Level	Change
		1	2	3	4	5	6	7	8
2004	29 Apr.	3.25	-	6.25	-	8.75	-	12.25	-
	12-May	3.00	-0.25	6.00	-0.25	8.50	-0.25	12.00	-0.25
	24 Jun.	2.75	-0.25	5.75	-0.25	8.25	-0.25	11.75	-0.25
	28 Jul.	2.50	-0.25	5.50	-0.25	8.00	-0.25	11.50	-0.25
	04 Nov.	2.25	-0.25	5.25	-0.25	7.75	-0.25	11.25	-0.25
2005	31 Mar.	2.00	-0.25	5.00	-0.25	7.50	-0.25	11.00	-0.25
	27 Jul.	3.25	1.25	5.00	-	6.75	-0.75	11.00	-
2006	12 Jul.	3.50	0.25	5.25	0.25	7.00	0.25	11.25	0.25
	30 Nov.	3.75	0.25	5.50	0.25	7.25	0.25	11.50	0.25
2007	28 Jun.	4.00	0.25	5.75	0.25	7.50	0.25	11.75	0.25
	27 Sep.	4.25	0.25	6.00	0.25	7.75	0.25	12.00	0.25
	30 Nov.	4.50	0.25	6.25	0.25	8.00	0.25	12.25	0.25
2008	24 Dec.	4.50	-	6.25	-	7.00	-1.00	12.25	-
2009	28 Jan.	4.50	-	6.25	-	7.00	-	12.25	-
	29 Jan.	4.00	-0.50	5.75	-0.50	6.50	-0.50	11.75	-0.50

Source: Bank of Albania

7. EXTERNAL SECTOR STATISTICS

7.1 BALANCE OF PAYMENTS (EUR millions)

Current Account														
				Trade Balance			Services		Income		Private Transfers	Official Transfers		
				Export of goods (fob)	Import of goods (fob)	Credit	Debit	Credit	Debit					
	1	4	5	6	7	8	9	10						
2005	-589.1	530.2	-2,006.9	-1,476.7	967.3	-1,107.7	168.2	-37.0	835.5	61.4				
2006	-471.0	630.7	-2,289.6	-1,659.0	1,156.6	-1,188.1	263.2	-54.4	968.1	42.5				
2007	-831.0	786.3	-2,890.4	-2,104.0	1,415.2	-1,402.3	278.6	-61.4	982.8	60.1				
2008	-1,290.6	915.9	-3,331.4	-2,415.5	1,524.0	-1,538.6	468.4	-159.0	802.9	27.2				
Capital Account				Financial Account					Net Errors and Omissions	Overall Balance	Reserve Assets	Total change in Reserve Assets	Of which: Revaluation	
				Direct Investment	Portfolio Investment	Other Capital*	Use of Fund Credit and Loans							
	11	12	13	14	15	16	17	18	19	20	21			
2005	99.2	351.8	209.3	-2.0	135.1	9.4	262.9	124.8	-124.8	-47.4	-77.4			
2006	143.4	415.0	250.3	27.2	131.8	5.8	119.2	206.6	-206.6	-159.2	-47.9			
2007	90.1	758.3	470.1	18.5	264.2	5.5	131.2	148.6	-148.6	99.1	-49.6			
2008	78.2	1,477.6	619.2	-69.2	932.7	-5.2	-73.2	191.9	-191.9	218.4	26.5			

Source: Bank of Albania

*Does not include Fund credit and loans

7.2 GEOGRAPHICAL BREAKDOWN OF EXPORTS OF GOODS* (EUR millions)

	European Union												
	Total	Austria	Belgium	United Kingdom	Denmark	Finland	France	Germany	Greece	Ireland	Italy	Luxembourg	Netherlands
	1 = sum of 2 to 16	2	3	4	5	6	7	8	9	10	11	12	13
2004	436.57	1.64	0.29	0.16	0.14	0.02	2.49	15.03	58.39	0.01	354.63	-	0.86
2005	466.67	1.22	0.26	0.72	0.20	-	3.67	17.61	55.42	-	383.92	-	0.72
2006	553.53	1.78	0.46	0.49	0.35	0.01	4.41	19.91	60.65	0.10	457.91	0.02	1.36
2007	642.90	1.91	0.33	1.79	0.17	0.14	4.91	19.20	65.02	-	534.99	0.22	0.45
2008	714.61	6.21	0.37	0.58	0.35	3.41	7.70	24.54	80.30	6.87	565.77	0.00	13.26
	Countries of the region												
	Total	Bulgaria	Bosnia and Herzegovina	Croatia	Serbia and Montenegro	Serbia	Montenegro	Macedonia FYR	Romania	Turkey	Others		
	1 = sum of 2 to 10	2	3	4	5	6	7	8	9	10	11	12	13
2004	19.16	1.28	0.31	0.32	1.84	-	-	6.04	0.18	9.19	-	-	-
2005	27.15	2.92	0.89	0.15	4.47	-	-	8.33	1.28	9.11	-	-	-
2006	34.98	2.64	3.44	1.77	8.54	-	-	10.07	0.52	8.00	-	-	-
2007	65.08	5.43	3.15	0.73	-	14.10	3.49	18.51	2.37	17.30	-	-	-
2008	74.70	6.59	1.53	1.54	-	0.52	19.00	26.99	1.48	17.05	-	-	-

Source: General Customs Directorate

*External trade statistics are compiled according to balance of payments methodology. Exports are in f.o.b. values.

7.3 EXPORTS BY PRODUCT GROUPS (SITC)(EUR millions)

	Total										
	Food and live animals	Beverages and tobacco	Crude materials, inedible, except fuels	Mineral fuels, lubricants and related materials	Animal and vegetable oils, fats and waxes	Chemicals and related products, n.e.s.	Manufactured goods classified chiefly by material	Machinery and transport equipment	Miscellaneous manufactured articles	Commodities and transactions not classified	
	2	3	4	5	6	7	8	9	10	11	
	1 = sum of 2 to 11	485.58	19.84	7.61	13.17	0.28	2.82	97.31	19.09	306.97	-
2004		485.58	19.84	7.61	13.17	0.28	2.82	97.31	19.09	306.97	-
2005		530.19	20.42	9.63	15.36	0.23	4.78	114.31	22.16	317.69	-
2006		630.74	26.77	8.34	27.27	0.44	6.22	141.51	24.50	360.85	-
2007		786.34	28.43	11.04	62.47	0.73	8.20	167.40	33.06	399.41	-
2008		915.87	32.27	2.63	81.47	0.21	10.33	231.91	37.95	411.35	-

Source: General Customs Directorate

*External trade statistics are compiled according to balance of payments methodology. Exports are in f.o.b. values.

7.4 GEOGRAPHICAL BREAKDOWN OF IMPORTS OF GOODS* (EUR millions)

	European Union											
	Total	Austria	Belgium	United Kingdom	Denmark	Finland	France	Germany	Greece	Ireland	Italy	Luxembourg
	1 = sum of 2 to 16	2	3	4	5	6	7	8	9	10	11	12
2004	1,190.25	20.47	14.33	10.45	4.15	3.93	25.66	113.81	340.91	5.89	596.61	0.60
2005	1,258.03	35.86	15.87	18.21	4.03	11.44	25.34	112.79	346.16	8.90	610.76	0.87
2006	1,385.32	28.97	20.40	33.63	3.63	6.22	23.08	136.18	380.66	7.41	677.25	0.75
2007	1,647.24	39.65	10.21	37.61	3.75	10.19	30.16	166.87	444.40	8.43	826.24	2.22
2008	1,925.61	45.33	10.10	36.94	4.90	12.86	42.57	215.63	522.93	7.06	944.38	0.42

	Countries of the region									
	Total	Bulgaria	Bosnia and Herzegovina	Croatia	Serbia and Montenegro	Serbia	Montenegro	Macedonia FYR	Romania	Turkey
	1 = sum of 2 to 10	2	3	4	5	6	7	8	9	10
2004	229.51	36.94	0.91	23.80	10.67	-	-	19.14	7.96	130.09
2005	296.49	59.18	2.70	24.99	13.16	-	-	25.83	15.31	155.32
2006	392.10	66.30	6.55	34.59	21.58	-	-	38.85	41.87	182.36
2007	452.84	54.29	9.19	29.67	-	63.70	2.59	59.08	13.06	221.26
2008	432.15	68.44	10.31	35.54	-	0.35	6.03	78.80	19.36	213.32

Source: General Customs Directorate

*External trade statistics are compiled according to balance of payments methodology. Imports are in c.i.f. values.

7.5 IMPORTS BY PRODUCT GROUPS (SITC) (EUR millions)

	Total										
	Food and live animals	Beverages and tobacco	Crude materials, inedible, except fuels	Mineral fuels, lubricants and related materials	Animal and vegetable oils, fats and waxes	Chemicals and related products, n.e.s.	Manufactured goods classified chiefly by material	Machinery and transport equipment	Miscellaneous manufactured articles	Commodities and transactions not classified	
	1 = sum of 2 to 11	2	3	4	5	6	7	8	9	10	11
2004	1,830.51	266.09	61.51	58.81	141.10	26.53	166.62	427.48	431.48	250.89	-
2005	2,083.85	272.31	64.71	75.92	181.75	28.49	201.77	509.84	488.98	260.09	-
2006	2,410.91	320.88	77.34	86.12	254.92	31.52	252.49	618.22	484.68	284.71	-
2007	3,044.71	379.30	89.38	68.16	446.38	33.96	302.23	754.90	630.91	339.50	-
2008	3,555.72	422.61	112.99	74.37	564.34	51.89	346.40	848.29	781.07	353.75	-

Source: General Customs Directorate

*External trade statistics are compiled according to balance of payments methodology. Imports are in c.i.f. values.